

Before the
Library of Congress
Copyright Office
Washington, D.C.

In the Matter of)
)
Verification of Statements of Account) Docket No. 2012-5
Submitted by Cable Operators and)
Satellite Carriers)
)
Notice of Proposed Rulemaking)

COMMENTS



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I. INTRODUCTION

The American Cable Association (“ACA”) files these comments in response to the Copyright Office’s Notice of Proposed Rulemaking (“NPRM”) in the above referenced docket.¹ The NPRM proposes regulations to implement provisions in the Satellite Television Extension and Localism Act of 2010 (“STELA”) that will allow copyright owners to audit certain Statements of Account (“SOAs”) filed with the Copyright Office.² In these comments, ACA addresses two specific proposals contained in the NPRM: (i) audit cost-shifting if the auditor concludes that there was an underpayment by a statutory licensee of five percent or more; and (ii) a two-week response period for a statutory licensee subject to audit to register concerns with audit results.³

First, ACA submits that the Copyright Office should not permit the shifting of an audit’s cost to a statutory licensee (i.e. the cable operator). Audits are generally burdensome procedures, especially for the audited company. The audit process proposed in the NPRM allows for a potentially lengthy back-and-forth process between the auditor and the statutory licensee, a process that would appear to cost thousands of dollars. In view of the fact that licensors have the choice of whether to seek an audit, and may join together to share in its cost, whereas licensees are involuntarily subjected to audits and could have to bear the costs on an individual basis, it would be inequitable to include a provision for audit cost-shifting.

The inequity of cost-shifting would be exacerbated by the proposed five percent underpayment threshold for cost-shifting, which can result in a relatively small royalty underpayment giving rise to an audit bill several orders of magnitude larger. Specifically, if the

¹ *In the Matter of Verification of Statements of Account Submitted by Cable Operators and Satellite Carriers*, Notice of Proposed Rulemaking, Docket No. 2012-5, 77 FR 35643 (rel. June 14, 2012) (“*Copyright Audit NPRM*”).

² *Id.* at 35649.

³ *Id.* (“The Office also welcomes comment on whether two weeks would be a sufficient amount of time for the statutory licensee to prepare a written response to the auditor’s report.”).

Copyright Office adopts a cost-shifting mechanism, it must set the cost-shifting threshold for cable operators significantly higher than five percent. Moreover, to avoid a disproportionate impact, the Copyright Office must provide some form of relief to smaller cable operators, such as setting the threshold for an underpayment only upon surpassing a minimum dollar amount. In the alternative, or in conjunction with establishing a higher cost-shifting threshold, the Copyright Office should establish an upper limit on the amount that a small cable operator would be responsible for paying for any audit.

Moreover, under the proposed audit procedures, a cable operator that disagrees with any of the auditor's facts or conclusions would have the burden of raising those issues during its initial consultation with the auditor, and responding within two weeks if the facts or conclusions remain in dispute.⁴ This is an unreasonably short response period, particularly for smaller cable operators. ACA therefore urges the Copyright Office not to limit the cable operator's proposed response time to two weeks.

In summary, ACA urges the Copyright Office to (i) not allow cost-shifting; (ii) provide relief to smaller cable operators if the Copyright Office does allow cost-shifting; and (iii) not limit the time a cable operator has to respond to an auditor's report to two weeks.

⁴ *Id.* ("If the statutory licensee disagrees with any of the facts or conclusions set forth in the auditor's report, the licensee's designee must raise those issues during the initial consultation with the auditor. If the auditor agrees that a mistake has been made, he or she should correct those errors before the report is delivered to the copyright owner(s). If facts or conclusions set forth in the report remain in dispute after the consultation, the licensee may provide the auditor with a written response setting forth its views. The licensee's deadline for providing this response would be two weeks (e.g., 14 calendar days) after the date of the initial consultation between the auditor and the licensee's representative.").

II. THE COPYRIGHT OFFICE SHOULD NOT PERMIT COPYRIGHT OWNERS TO SHIFT AUDIT COSTS TO STATUTORY LICENSEES

A. Audit Cost Shifting Would Be Extremely Burdensome for Smaller Cable Operators

In the NPRM, the Copyright Office invites comment on whether the regulation should include a cost-shifting provision, and if so, whether the percentage of underpayment needed to trigger cost-shifting to the statutory licensee should be more or less than five percent.⁵ ACA strongly recommends that the Copyright Office not include a cost-shifting provision in its final regulations implementing audits as required by STELA.

ACA submits that, in general, audits are burdensome, especially for the audited party. The NPRM proposes a lengthy back-and-forth process that would likely involve a significant amount of operator and auditor time. While the proposed regulations give copyright owners the opportunity to join in the audit, and to share the costs of the audit among each other,⁶ under the cost-shifting proposal the audited cable operator could be held solely responsible for the auditor's fee. Consequently, in contrast to the copyright owners, cost-shifting would expose a cable operator to substantial costs. If a copyright owner does not wish to assume the risk of paying for an audit, it may decide against initiating, or joining, one. A cable operator, conversely, does not have the same opportunity to call for the audit or decide against one to avoid the risk of bearing the costs. Given that the proposed regulations give copyright owners the right to both request an audit and the opportunity to minimize their costs by sharing them with other owners, it is only fair for copyright owners to assume all of the costs of an audit regardless of the outcome.

⁵ *Id.*

⁶ *Id.* at 35646 (“Copyright owners that join in the audit would...be required to pay for the auditor for his or her work in connection with the audit.”).

The costs of an audit can be significant for cable operators, particularly smaller operators. Imposing audit costs on smaller cable operators would conflict with the recommendations of the Copyright Office to minimize the administrative burdens of the compulsory license process in its periodic reports.⁷ Accordingly, ACA recommends that the Copyright Office not include a cost-shifting provision in its proposed regulations. By not adopting a cost-shifting provision, the Copyright Office will likely reduce the number of groundless audits of smaller cable operator SOAs because licensors may be less likely to seek audits in cases where the potential benefit of finding some minimal discrepancy (e.g., a difference in payment of just tens of hundreds of dollars) is far outweighed by the cost of the audit itself. This will help ensure a reasonable and proportionate auditing system.

B. If the Copyright Office Permits Cost-Shifting, it Must Adjust its Proposal to Decrease Burdens on Smaller Cable Operators

The NPRM asks whether the percentage of underpayment needed to trigger shifting the cost of the audit to the statutory licensee should be more or less than five percent.⁸ As discussed above, it is ACA's position that the Copyright Office not include any level or form of cost-shifting in its audit rules. Nonetheless, if the Copyright Office includes a cost-shifting provision, the underpayment threshold either should be set significantly higher than five percent or should be based on the underpayment surpassing a minimum dollar amount, and the Copyright Office must provide additional relief to smaller cable operators.

⁷ See, e.g., *A Review of the Copyright Licensing Regimes Covering Retransmission of Broadcast Signals*, A Report of the Register of Copyrights at 41-42 (Aug. 1, 1997) ("*1997 Report*") ("[T]he administrative complexity of the current cable rates is burdensome, and in many respects, unfair. Many hours are spent by cable systems just to understand how much they owe and how to fill out the forms (which often requires legal advice)."); *Satellite Home Viewer Extension and Reauthorization Act, Section 109 Report*, U.S. Copyright Office, at 106 (2008) ("*2008 Report*") ("[T]he royalty structure should be simplified to make it administratively efficient for users of the license, copyright owners, and Copyright Office examiners.").

⁸ *Copyright Audit NPRM* at 35649.

For smaller cable operators, the Copyright Office cost-shifting proposal for cases of underpayments of more than five percent is particularly inequitable, especially given the relatively small amounts of fees paid to the Copyright Office by these operators. With no prescribed limit on audit costs, smaller operators could be required to cover audits costs that far exceed in actual dollars a five percent underpayment in royalties.

For example, a cable operator filing a long-form SA-3 with \$527,601 in gross revenues (gross revenues under \$527,600 require only filing a short-form SA-1/2) at the minimum fee level would pay \$5,614 in royalties. Five percent of \$5,614 is \$280. In this situation, the Copyright Office's proposed regulations would require a cable operator to cover an auditor's fee for an underpayment that totals \$280 or more, while the auditing copyright owners can share the cost among each other if the underpayment totals \$280 or less.

At these royalty fee levels, a five percent underpayment could require an operator paying far more for an audit than it must pay to the Copyright Office for the reported underpayment. It is inequitable to subject an individual cable operator to potentially thousands of dollars in auditing costs for a small underpayment, which amounts to a miniscule percentage of the total amount of royalties that the Copyright Office collects from all cable operators.

Since the inception of the compulsory license, Congress and the Copyright Office have taken account of disproportionate burdens of its rules on smaller cable operators, who serve smaller numbers of subscribers and typically have more limited financial resources.⁹ First, smaller systems are permitted to pay reduced fees.¹⁰ Second, smaller systems are permitted to

⁹ "Congress explained in 1976 why it was affording the smaller cable systems lower rates and unlimited importation of distant signals: 'Because many smaller cable systems carry a large number of distant signals, especially those located in areas where over-the-air television service is sparse, and because smaller cable systems may be less able to shoulder the burden of copyright payments than larger systems, the Committee decided to give [smaller cable systems] special consideration.'" *2008 Report*, n.73 quoting H.R. Rep. No. 1476, at 96-97.

¹⁰ A Review of the Copyright Licensing Regimes Covering Retransmission of Broadcast Signals, U.S. Copyright Office, at 42 (1997).

carry adjacent market signals without a sharp increase in royalties.¹¹ Moreover, Congress understood that, as a general matter, smaller cable systems likely would be less able to pay the same fees as charged to larger systems.¹²

Like Congress, the Copyright Office historically has been willing to take account of the fact that some cable operators have more limited financial resources than others, particularly smaller cable operators. For example, in 2008, the Copyright Office stated that “small cable operators should continue to be treated differently under the statute because they provide a needed service and operate under economic constraints that are vastly different from those affecting larger operators.”¹³ Moreover, in 2006, the Copyright Office acknowledged that with mandatory electronic payment, “there may be circumstances which would make it virtually impossible for a remitter to use the electronic payment option or would work a financial or other hardship.”¹⁴ Consequently, the Copyright Office amended its regulations to include a waiver provision.¹⁵ Further, the Copyright Office has recognized that increased copyright fees for small cable systems limited operating cash flow and raised concerns that increased fees could lead to such systems dropping distant broadcast signals.¹⁶ In 2011, the Copyright Office again expressed concern about the impact of its recommendations on cable operators with limited

¹¹ *Id.* (in recognition of the fact that these systems are typically located in areas where consumers cannot receive off-air television service and usually carry a larger number of distant signals).

¹² *Id.*

¹³ *2008 Report* at 121.

¹⁴ *In the Matter of Electronic Payment of Royalties*, Final Rule, Docket No. RM 2006-4, 71 FR 45739 at 45739 (Aug. 10, 2006).

¹⁵ *Id.*

¹⁶ *Id.*; *1997 Report* at 43.

resources, particularly smaller ones.¹⁷

Consistent with the foregoing, if the Copyright Office adopts a cost-shifting provision in its audit rules, it must also adopt measures that provide relief for smaller cable operators. Without relief for smaller cable operators, these companies would need to devote significant administrative (and potentially financial) resources to monitoring audits, reviewing the auditor's facts and conclusions, and prepare for the consultation and response requirement. As the Copyright Office itself has acknowledged, smaller cable operators are sometimes financially fragile.¹⁸ Accordingly, to the extent the Copyright Office provides for cost-shifting in its final regulations, it must provide smaller operators with relief from the disproportionate burden cost-shifting would impose on them.

Finally, although small cable operators should not be subject to any cost shifting under any circumstance, should the Copyright Office nonetheless adopt a cost-shifting provision, it must set the threshold for cost-shifting for small cable operators significantly higher than five percent, or base the threshold on an underpayment surpassing a minimum dollar amount. In the alternative, or in conjunction with establishing a higher cost-shifting threshold, the Copyright Office should establish an upper limit on the amount that a small cable operator would be responsible for paying for any audit.

¹⁷ Satellite Home Viewer Extension and Reauthorization Act, Section 302 Report, U.S. Copyright Office, at 139 (2011) ("Before determining the date-specific trigger and transition period for the phase-out of the distant signal licenses, the Copyright Office recommends that Congress evaluate the concerns of stakeholders who operate with limited resources in the broadcast programming distribution chain and determine whether special consideration is advisable.").

¹⁸ See *1997 Report* at 43; *2008 Report* at 121.

III. THE PERIOD FOR RESPONDING TO AUDIT RESULTS MUST BE LENGTHENED

The NPRM invites comment on whether two weeks would be a sufficient amount of time for a statutory licensee to prepare a written response to the auditor's report.¹⁹ ACA submits that the Copyright Office must not limit a cable operator's response time to two weeks.

As noted above, the Copyright Office has periodically recommended simplifying the compulsory license process and related administrative burdens. A two-week response limit would serve only to increase administrative burdens, especially for smaller cable operators with limited resources, contrary to the Copyright Office's recommendations. To meet with an auditor, review the auditor's report, and prepare a written response setting forth its views, all within two weeks, a cable operator would need to devote significant administrative resources to reviewing the auditor's report, preparing a response, drafting, and submitting the response to the auditor. Depending on the complexity of the disputed issues, the cable operator may also need to devote significant financial resources to retain outside legal or accounting assistance, for which two weeks may not be sufficient to allow a complete review of the issues at hand.

As a result, ACA submits that two weeks to respond and dispute an auditor's facts or conclusions is not sufficient, especially for smaller cable operators. Consequently, to give cable operators a better opportunity to respond to an audit, ACA recommends that the Copyright Office provide cable operator's flexibility to respond within a reasonable amount of time.²⁰

IV. CONCLUSION

ACA submits that the Copyright Office should not permit the shifting of an audit's cost to the cable operator in any situation. The fact that statutory licensees could have to bear their costs individually while licensors, regardless of the outcome of the audit, may join together to

¹⁹ *Copyright Audit NPRM* at 35649.

²⁰ Other Copyright Office audit regulations do not reference any limit on the time an audited party may respond to an auditor's report and dispute facts or conclusions, other than to require an initial consultation. See, e.g., 37 C.F.R. §§ 261.6(f), 261.7(f), 380.6(f), 382.16(f), 384.7(f).

participate in an audit, thus from the outset lowering their potential costs, makes it inequitable to include a provision for audit cost-shifting under any circumstance. This inequity would be compounded by the NPRM's proposed five percent underpayment threshold for cost-shifting, which can amount to a relatively small amount of money for smaller cable operators compared to the cost of an audit. Should the Copyright Office nonetheless permit audit cost-shifting, the threshold should be set significantly higher than five percent, and relief must be afforded to smaller cable operators by limiting their potential audit costs. Finally, to ameliorate these burdens and give cable operators a better opportunity to respond to an audit, the Copyright Office should not limit the cable operator's proposed response time to two weeks.

Respectfully submitted,



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