

**Before the  
COPYRIGHT OFFICE  
LIBRARY OF CONGRESS  
Washington, D.C.**

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<b>In the Matter of</b>	)	
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<b>Mechanical and Digital Phonorecord Delivery Compulsory License, Statement of Accounts</b>	)	<b>Docket No. 2012-7</b>
	)	

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The National Music Publishers’ Association (“NMPA”), including its wholly owned licensing subsidiary, The Harry Fox Agency, Inc. (“HFA”), Church Music Publishers’ Association (“CMPA”), Nashville Songwriters Association International (“NSAI”), and the Songwriters Guild of America (“SGA”) respectfully submit these Reply Comments pursuant to the Copyright Office’s Request for Additional Comments to amend regulations for reporting monthly and annual Statements of Account for the making and distribution of phonorecords under the Section 115 compulsory license. 78 Fed. Reg. 78309 (December 26, 2013).

NMPA and HFA have participated in this inquiry by filing joint Comments with the Digital Music Association (“DiMA”), Recording Industry Association of America, Inc. (“RIAA”), and Music Reports, Inc. (“MRI”).<sup>1</sup> NMPA, HFA, CMPA, NSAI and SGA (collectively referred to herein as “the Songwriter Parties”) now wish to offer additional comments on a few points raised by MRI regarding the certification requirements set forth in Section 115 (c)(5) of the Copyright Act.<sup>2</sup>

**Introduction**

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<sup>1</sup> Joint Reply Comments of National Music Publishers’ Association, the Harry Fox Agency, Digital Music Association, Recording Industry Association of America, Inc., and Music Reports, Inc. in the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License (“Joint Reply Comments”), available at [http://www.copyright.gov/docs/docket2012-7/comments/reply/nmpa\\_hfa.pdf](http://www.copyright.gov/docs/docket2012-7/comments/reply/nmpa_hfa.pdf).

<sup>2</sup> Reply Comments of Music Reports, Inc. in the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License (“MRI Reply Comments”), available at <http://www.copyright.gov/docs/docket2012-7/comments/reply/mri.pdf>.

The Songwriter Parties described previously how Section 115 of the Copyright Act creates an honor system for licensing in which compulsory licensees self-license, self-report and self-assess. Certification of the Statements of Account is the only assurance that songwriters and music publishers have been paid properly for the use of their musical works under compulsory license. The Songwriter Parties, therefore, proposed a CPA certification in their reply comments filed on December 10, 2012 that requires CPAs to conduct an examination in accordance with the attestation standards established by the American Institute of Certified Public Accountants (the “Attestation Standards”)<sup>3</sup> of either the annual statements directly or the processes that generate annual statements (the “Songwriter Parties’ Certification Proposal” or “Proposal”).<sup>4</sup>

More specifically, the Songwriter Parties’ Certification Proposal requires a CPA engaged to certify a compulsory licensee’s Annual Statement of Account to conduct an “examination” that results in an “opinion” under the Attestation Standards. Under the AICPA’s Attestation Standards, use of these terms of art is significant. They mean that the Songwriter Parties are proposing that the CPA’s review provide a high level of assurance that copyright owners have been paid correctly.<sup>5</sup> Any lower level of review would not serve the purposes of the CPA certification requirement of Section 115 and, therefore, should be set as a matter of policy by the Office, not left to the discretion of the compulsory licensee and the CPA it engages. Whether the CPA examines the annual statements themselves or the processes that generate the annual statements is left up to the compulsory licensee and CPA. In addition, the procedures for testing the statements or processes are left up to the CPA, but, of course, governed by the Attestation Standards. Lastly, the Songwriter Parties’ Certification Proposal requires

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<sup>3</sup> The American Institute of CPAs Statements on Standards for Attest Engagements, § 101 Attest Engagements (“Attestation Standards”), *available at* <http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AT-00101.pdf>.

<sup>4</sup> Reply Comments of National Music Publishers’ Association, the Harry Fox Agency, the Nashville Songwriters Association International, and the Songwriters Guild of America in the Matter of Mechanical and Digital Phonorecord Delivery Compulsory License (“Songwriter Reply Comments”), Exhibit A, *available at* [http://www.copyright.gov/docs/docket2012-7/comments/reply/nmpa\\_fox.pdf](http://www.copyright.gov/docs/docket2012-7/comments/reply/nmpa_fox.pdf).

<sup>5</sup> Attestation Standards at § 101.65 (“The terms examination and review should be used to describe engagements to provide, respectively, a high level and a moderate level of assurance.”)

that, to the extent a compulsory licensee elects to provide a certification of the process used to generate Annual Statements, the responsibility for compliance with Section 115 and its attendant regulations be placed on the management of the compulsory licensee.

MRI's Reply Comments do not take issue with the general idea the music publishers and songwriters deserve a high level of assurance that they are being reported to and paid correctly. Instead, MRI's concerns appear to flow from its preference that third-party service providers be permitted to submit a CPA certification to songwriters and music publishers regarding the portion of the royalty accounting process the service providers handle separately from the certification required of the compulsory licensee itself. As a result, the compulsory licensee's certification would be limited to the information or data provided to the third-party service provider and it would not have responsibility for evaluating the processes used by the service provider or, if appropriate, the CPA report obtained by the third-party service.

## I.

### **MANAGEMENT OF THE COMPULSORY LICENSEE MUST BE RESPONSIBLE FOR THE ACCURACY OF STATEMENTS OF ACCOUNT EVEN WHEN THEY OUTSOURCE ADMINISTRATIVE FUNCTIONS**

#### **A. THE BULK DIGITAL LICENSING PROCESS**

A brief description of the role a third-party service provider, or administrator, plays in accounting for royalties paid pursuant to compulsory licenses may assist the Office in evaluating the current certification proposals. It can be summarized at a very general level in five steps:

1. Musical compositions catalog registration and management

The initial step in the process is for an administrator, such as HFA or MRI, to manage its song database by ingesting, on a daily basis, song catalog additions and other information, including ownership claims and disputes, business rules for usage and rules regarding payment, such as letters of direction, and information about estates and heirs.

## 2. Service of Notices of Intent

Next, the digital music service and the administrator exchange millions of lines of data regarding the sound recordings to be made available in the digital music service's repertoire and compare them to the compositions in the administrator's database in order to determine which recordings require service of a Notice of Intent. The administrator stores a record that links the composition subject to the Notice of Intent with the recordings in the digital music service's repertoire.

## 3. Updating licensing

Following the original data exchange, the process, is repeated regularly so that the digital music service can obtain compulsory licenses for additions to its repertoire.

## 4. Usage and Royalty Calculation

On a monthly basis, the digital music service sends a usage report consisting of millions of lines of data to the administrator. At the same time, it provides the relevant financial information for calculating the net royalty pool to be allocated based on the usage data. Such financial information includes, for example, gross revenue, label expenses, the number of paid subscribers and the performance royalty expense. The administrator then calculates the royalties due for the period and allocates royalties to particular compositions based on the usage data provided by the digital music service and the records it maintains linking such usage to compulsory licenses and compositions.

## 5. Royalty Reporting and Distribution

After the royalties are calculated and allocated to particular songs, the digital music service or its administrator (a) determines whom to pay with respect to each song, (b) generates the related royalty statements, (c) transmits those statements to the owners or administrators of the relevant songs, and (d) pays the appropriate party.

Each step in the process described above requires establishing a relationship, obtaining, formatting and exchanging sound recording, publishing and usage data, generating matches for both compulsory licensing and distributing royalties, updating that data on a regular basis and then

repeating the process in order to calculate and pay royalties accurately at any given moment in time. Accordingly, the accuracy of the resulting Statements of Account are dependent upon both the accuracy of the financial and usage data provided by the digital service provider and the accuracy of the calculation and allocation performed by the administrator. The use of a third-party administrator to process royalties and issue statements pursuant to compulsory licenses, therefore, raises four questions:

1. Is the financial data provided by the digital music service accurate?
2. Is the process used by the digital music service designed and operated effectively such that songwriters and music publishers can be confident the play-count is accurate?
3. Did the administrator calculate the royalties properly based on the financial data provided by the digital music service?
4. Is the process used by the administrator designed and operated effectively such that songwriters and music publishers can be confident that the net royalty pool is allocated and paid properly.

The Songwriter Parties' Certification Proposal requires the compulsory licensee's management to take responsibility for answering "yes" to each of the above questions, even if it outsources administration of its compulsory licensing process.

## **B. CPA's Test Management Assertions**

As discussed in the Songwriter Parties December 10, 2012 comments, assurance services are generally referred to as "attest engagements" by CPAs. Attest engagements are those in which a CPA is engaged to issue or does issue an examination or other report "on subject matter, or an assertion about the subject matter that is the responsibility of another party."<sup>6</sup> The Songwriter Parties

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<sup>6</sup> Attestation Standards at §101.01.

Certification Proposal, for example, contains the following assertions about the subject matter that would be tested by the CPA. It requires that the CPA has conducted an examination:

(I) of an assertion by management of the compulsory licensee that the processes, including the calculation of statutory royalties, it operated generated Annual Statements relevant to such examination that present fairly, in all material respects, both the compulsory licensee's usage of compulsory licensors' musical works under compulsory license during the fiscal year covered by such Annual Statements, the statutory royalties applicable thereto, and such other data as are relevant to the calculation of the statutory royalties applicable thereto in accordance with 17 USC § 115 and 37 CFR parts 210 and 385, as amended or superseded from time to time (collectively, the "Usage and Royalty Data"); and

(II) of an assertion by management of the compulsory licensee that the internal controls relevant to the processes used to generate the Annual Statements prepared by or on behalf of the compulsory licensee were suitably designed and operated effectively during the period covered by the Annual Statements . . . ”<sup>7</sup>

In short, these assertions mean that the CPA is testing the digital music service's representation that it or its third party service provider reported royalties properly on Statements of Account issued pursuant to compulsory licenses. The CPA conducting the examination has the option of testing the third-party service provider's data, controls and processes directly or relying upon an appropriate report of another CPA who has examined the operations of the third party service provider. As discussed in the Songwriter Parties' December 10, 2013 Reply Comment, the AICPA has established specific standards for examining the processes operated by third party service providers on behalf of their customers that may be used by the customer or the customer's CPA.<sup>8</sup> See SOC Reports Information for Service Organizations.<sup>9</sup> In instances where a compulsory licensee outsources services related to the processing of compulsory licenses, monthly, or annual reports, therefore, the compulsory licensee and the CPA it engages to certify Annual Statements will have the ability to rely upon an appropriate examination report issued by the service provider's CPA. Such reliance, however, is not blind. The compulsory licensee's CPA must review the third-party service provider's CPA report and

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<sup>7</sup> Songwriter Reply Comments, Exhibit A at 210.17(f)(2)(ii)(A).

<sup>8</sup> Songwriter Reply Comments at 18.

<sup>9</sup> Service Organization Controls (SOC) Reports for Service Organizations, *available at* <http://www.aicpa.org/interestareas/frc/assuranceadvisoryservices/pages/serviceorganization'smanagement.aspx>.

make an independent judgment that the examination conducted was sufficient to rely upon in the context of its own examination of the compulsory licensee.<sup>10</sup> Regardless of which approach is used, management of the compulsory licensee is still responsible for ensuring compliance with Section 115 and its attendant regulations and the CPA confirms such compliance.

The MRI proposal substitutes an assertion by management of the third-party administrator for that of the actual compulsory licensee. The Songwriter Parties believe this is inappropriate for two reasons. First, it removes responsibility for at least a portion of the process used to generate Statements of Account from management of the compulsory licensee. Second, the third-party service provider is not in privity with the songwriters or music publishers who are subject to the relevant compulsory licenses. As a result, it is unclear what recourse a songwriter or music publisher would have if it believes Statements of Account were inaccurate, even though certified by the third-party administrator's CPA. In an honor system where the CPA's certification is the only check on compulsory licensees, placing responsibility for compliance with Section 115 and its attendant regulations directly and solely on management of the compulsory licensee provides the strongest incentive for accurate payment and reporting of statutory royalties.

## II.

### **THE SONGWRITER PARTIES' CERTIFICATION PROPOSAL IS SUFFICIENTLY FLEXIBLE TO ALLOW CPAs TO PERFORM THEIR EXAMINATION EFFICIENTLY**

The conclusions required by the opinions set forth in the Songwriter Parties's Certification Proposal is that the Annual Statements themselves or the processes that generated the Annuals Statements complied in all material respects with Section 115 and related regulations.<sup>11</sup> In addition, the Parties' proposal includes the required assertions and a description of the examination procedures

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<sup>10</sup> Songwriter Reply comments, Exhibit A.

<sup>11</sup> Songwriter Reply Comments, Exhibit A at § 210.17(f)(2)(ii)(C).

that comply with the Attestation Standards.<sup>12</sup> The examination resulting in these conclusions must be conducted pursuant to the Attestation Standards. They require the CPA to conduct comprehensive field work to collect “sufficient evidence” providing a reasonable basis for the conclusion that is expressed in the report.<sup>13</sup> Where appropriate, they may also require written representations from the responsible party.<sup>14</sup> Under these standards, however, CPAs exercise professional judgment when determining the process for collecting evidence and the types of evidence that are sufficient to support the their opinions.

### **CONCLUSION**

By requiring examinations as set forth in Exhibit A of the December 10, 2012 Reply Comments that result in one of the alternative opinions, the Songwriter Parties’ proposed regulations place the responsibility for compliance on the management of the compulsory licensee while providing the high level of review necessary to ensure management of the compulsory licensee takes such responsibility seriously. This rigor is accomplished without unduly limiting the flexibility of compulsory licensees to operate their business using internal or external resources and relies upon the exercise of professional judgment by CPAs engaged by the compulsory licensee.

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<sup>12</sup> Songwriter Reply Comments, Exhibit A at § 210.17(f)(2)(ii)(A).

<sup>13</sup> Attestation Standards at §§ 101.51-58

<sup>14</sup> Attestation Standards at §§ 101.59-62.



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Respectfully submitted,



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