



# Internet Corporation for Assigned Names and Numbers

19 May 2004

Bhavin Turakin, Chairman & CEO  
Directi.com

Dear Bhavin:

Thank you for your letter outlining the concerns you have with the proposed ICANN Budget. It is clear and well thought out. I know that your letter was addressed to Vint Cerf. Vint and I communicated to determine an appropriate response and he has contributed to the composition of this letter.

Please know that the ICANN staff put a great deal of thought and work into the proposed budget model. That effort included considerable discussion of the effects of rate increases on large and small registrars, barriers to entry, and the DNS marketplace.

Please take this response to your paper as constructive discussion and not argument. The ICANN staff, board and various constituencies discussed several finance models and their effects on the ICANN budget and on the community. Many hours were spent in this activity – just as are you doing now. Many of the arguments you make were considered – most were adopted as part of the plan.

First, the lack of public forum you mentioned has been cured. It was under construction when ICANN received your letter. It will be posted.

On the more important issues:

As you probably recognized from the budget document, the per annum fee was developed in recognition of the fact that while some of ICANN's effort resulting from relationships with registrars is proportional to the size of the registrar, significant other effort expended on behalf of registrars is fixed for each registrar regardless of the number of names registered.

An example of this latter activity is ICANN addressing issues with contractual compliance. There are costs related to consumer protection and compliance activities that do not vary with the number of names under registration. ICANN invests to maintain linkages with various government agencies to protect consumers and help ICANN do a better job of assuring that all registrars follow the rules of the road in fair fashion. As ICANN adopts a more proactive contractual compliance program during the next fiscal year, activities will incur per registrar, rather than per name expenses.

Other activities include administration of various databases and responses to business and technical queries.

So while ICANN proposed that some of the costs be allocated on a per registrar basis and that some form of such an allocation is fair, I take your queries to center around the question of whether the allocation methodology in the budget is fair. ICANN submits that it is fair, asks that you consider the following, and then asks that we continue the dialogue so that a consensus is reached.

### **Effect on smaller registrars**

ICANN believes that smaller registrars will not be forced to leave the market place for two reasons:

- 1) Many or most of the smaller registrars can easily afford the fee due to revenues received by use of access to the batch pool, and
- 2) The fee will be mostly forgiven for those registrars that do not employ their right to access the batch pool and for whom the fee would severely affect the ability to carry on.

To the first point, it has been estimated by others that over 110 registrars presently derive revenue from using or selling their contractual right to access the batch pool in an effort to register deleted names. That revenue has been estimated at \$20,000 to \$30,000 per month for, in the words of one registrar, sitting and doing nothing. (These activities should be contrasted with the business models of registrars conducting standard marketing and registration operations where margins and revenue streams are tighter.)

There are a number of accreditation applications in the pipeline, including several with clear indications that the accreditation is to be used to gain access to the batch pool. ICANN anticipated none of those applicants will withdraw their application based upon the new fee structure. As stated in an earlier registrar posting concerning the budget, none of the existing registrars earning over \$240,000 annually should protest the fee.

ICANN does not condone the use of accreditations that are used strictly for access to secure deleted names. In fact, when faced with an abnormally large spate of accreditation applications, ICANN temporarily halted the accreditation process and convened an emergency session of the ICANN Board to discuss whether large number of accreditations should be granted in an environment where so many new accreditations were intended solely to access the batch pool.

With regard to the second point, forgiving fees in certain circumstances will avoid situations forcing smaller registrars out of the market.

One registrar posting inferred that smaller registrars might be better off as resellers rather than have to bear the burden of fees as an accredited registrar. While this may be true in some cases, ICANN also recognizes that several small registrars, especially those outside the United States, play a meaningful role in the DNS community.

As soon as the per annum fee was postulated, ICANN staff began discussing alternatives for fair, bright line rules for establishing forgiveness. One registrar posting suggested that ICANN developed the theory in a knee jerk reaction to comments made during the Budget Advisory Group meeting and had no ideas for creating the rules for such a procedure.

This is not true. As stated above, ICANN considered the issue ever since the per annum fees were suggested. Forgiveness was not included in an earlier version of the budget because many in the community stated that it was too difficult to develop a fair method that could not be "gamed." After discussion before and during the Budget Advisory group meeting, ICANN worked on developing a model that is fair and predictable.

The model was not included in the budget posting because it is still being tested with the opinions of various technical and business experts in the community. That testing continues. The model will first be built around determining which registrars are realizing revenues through use of the batch pool. At this point, it can be said that the model will require those receiving substantial revenue by hitting the batch pool to pay the per annum fee and that those registrars can be clearly and easily identified through the numbers and types of transactions incurred.

The second part of the model, will judge whether the financial status and business model of the registrar require some relief. I believe through interactions such as these exchanges of information, the best model will be devised. In any case, it is ICANN's position that deserving registrars should retain their accreditation.

The fees suggested in the budget indicate that qualifying registrars would pay approximately \$10,000 annually (the \$4,000 accreditation fee plus a per annum fee of approximately \$6,000) and be granted the ability to sell names from all registries, including anticipated new sTLDs.

### **Effects on larger registrars**

I understand your viewpoint that under the present scenario, larger registrars will save a huge amount of money compared to a budget where they would be paying 37 cents a transaction instead of 25 cents.

Looking at the other side of the same coin, the larger registrars (and all registrars) are paying at least 7 cents per transaction more than in the present budget year. Using the numbers developed on your spreadsheet, NSI is being asked to pay \$536K more than last year, Tucows \$273K more, GoDaddy \$253K more and so on. It is true that these amounts are smaller percentage increases than paid by smaller registrars, but these amounts can materially affect the business model of the larger registrars.

The fairness argument applies equally to these registrars. The larger registrars are paying 40-50% increases in fees and that increase is applied to a numerically large base. Your model suggests it is fairer that the larger registry fee increase should be as high as \$1.4MM or 108%.

In the cases of smaller registries, the six-figure increases heads asymptotically to the \$20-\$30K range in fairly rapid order. As discussed above, most of these registrars derive significant revenue from sources other than the straight registration of domain names and can afford the fee. Many others can be forgiven a large portion of the fee.

As in all fairness discussions, the topic of a judging the percentage of a big number against a percentage of a small number must be considered. In the ICANN proposed model it was thought that the larger registrars were paying a considerable increase by any standard while the smaller registrars' payments were increased by amounts consistent with their business models.

### **Effects on the ICANN budget**

If the programs described in the ICANN budget are effectively implemented, many registrars should not abandon their accreditation. In fact, and based upon the number of accreditation applications in queue, ICANN expects the number of accreditations to increase significantly between now and the start of the fiscal year. There are indications in these applications that most of these new registrars will derive significant income through their access to the batch pool. As stated above, ICANN does not condone this business model but a special meeting of the board concluded that applications could not be denied based upon apparent business model absent substantial more study into this subject matter. As I stated earlier, ICANN estimates that none of the existing applications for this purpose will be withdrawn given the new fee structure.

Similarly, new registrars will not be precluded from forgiveness at the time of the first quarterly invoicing. ICANN does stand for promotion of competition. It is also understood however, that potential registrars should have robust financing and a solid business plan before entering the field. (As counterpoint to your discussion, when larger registrars discussed potential resources, it was offered that a \$17-\$19K fee should be reasonable to an ongoing, robust registrar operation.)

Given all this, it is anticipated that ICANN will have over 250 accredited registrars by the start of the fiscal year. The increased numbers should ensure the planned for revenue stream while allowing some reductions in rates to the smaller registrars.

### **Effects of new sources of revenue**

ICANN agrees with every registrar posting regarding the generation of new sources of revenue. ICANN's business model should not be based on sole or few sources of revenue. It is not sound practice. New sources of revenue are intended to limit any increases to the registrar fees and to reduce them. Those revenues will be realized in time for or before the following fiscal year.

Where the budget ascribed to holding the 25 cent fee constant, it should also be taken as making the same commitment to the per annum fee.

### **Conclusion**

I realize this writing does not address all your concerns. However, there is a basis from which to work. The fact that many small registrars have significant revenue streams means that there are not as many registrars adversely impacted by the fee structure as some may have thought. Also, I believe we can develop a method for waiver of a portion of the fees that is objective and does not result in differences and partiality.

Given the above two conditions above, a fair model can be created in a budget that: significantly increases cash fees from large registrars, charges registrars availing themselves of the batch pool a very reasonable fee, moves to forgive the debt of smaller registrars, adjusts to significant changes in the marketplace and plans for other sources of revenue.

Having written this document, I know the work that went into yours. Everyone at ICANN appreciates the passion that went into your effort and we all generally agree with your principles. As stated above, this document is not intended as an end. We are looking forward to your comments and those from the community.

Sincerely,

Kurt Pritz  
ICANN