



COMMENTS OF THE INTELLECTUAL PROPERTY CONSTITUENCY (IPC)

Replenishment Strategy for the ICANN Reserve Fund

April 25, 2018

The Intellectual Property Constituency (IPC) of the GNSO is pleased to submit comments on the Replenishment Strategy for the ICANN Reserve Fund. As stated in earlier comments, the IPC notes the challenges of replenishing ICANN's reserve after the IANA stewardship transition and commends ICANN in its attempts to provide transparency in this process. It is crucial that ICANN demonstrate to the world its fiscal responsibility and adherence to best practices when it comes to the reserves. Failure to do so could undermine ICANN's hard-fought independence from direct government oversight. With that in mind, IPC submits the following observations and recommendations.

1. Comments and Concerns Regarding the Proposed Replenishment Strategy

The IPC is encouraged by the recent actions of the ICANN org and Board to take definitive steps to address the problem of the reserves and recognize that the practice of withdrawing from the reserves must be curtailed with better controls set in place. The IPC recognizes the first and second consultation papers as steps in the right direction and offers our comments on the second consultation paper below.

1.1 First Consultation Paper and Agreed Target Level - The IPC notes that the agreed target level for the reserves has been set a minimum of 12 months and that the current reserve level has a shortfall of at least \$68 million USD. This one-year minimum threshold is supported by the IPC as the absolute minimum. The IPC notes that the 2007 target for the reserve fund was not met. In 2014, reserves were at 90% when the withdrawals began. This failure to adequately fund the reserves as agreed coupled with the profligate spending on legal fees for the IANA transition brought the ICANN reserve fund to dangerously low levels. It is a cautionary tale and should never happen again. The IPC supports the current target level for replenishment with the following advisory: Should the reserve gap increase; a different strategy may be required and the community consulted accordingly.

1.2 Second and Third Consultation Papers – IPC notes that this comment is in response to the Second Consultation Paper and that a Third Consultation Paper will be produced that focuses on governance of the fund. IPC looks forward to that paper as the current state of the reserves demonstrates poor governance that demands redress through tighter controls and more transparency into disbursements.

1.3 Shortfall – IPC notes that the predicted shortfall is based on the FY19 Budget. We hope that the Board and the ICANN org have heeded the IPC’s advice to base the figures on realistic assumptions of growth. Per the IPC comments on the FY19 Budget, the increase in revenue was based “*upon a best estimate increase in transaction fees from registries and registrars of approximately US\$3 million. However, no detailed assumptions for this increase are provided. Such important growth assumptions should be provided in greater detail.*”¹ ICANN org cannot afford to miscalculate or greater shortfalls could arise in the budget that will affect the organization’s ability to replenish the reserves in a timely and prudent manner.

1.4 Sources of Funding – The IPC supports looking to the contributions from ICANN org and leftover funds at the end of the new gTLD program as the best sources for reserve fund replenishment. We have concerns about using auction proceeds or additional funds from contracted parties. In terms of using the auction proceeds, the IPC notes that community is in the middle of a multi-stakeholder process (the CCWG on Auction Funds) that has been working hard for over a year on producing an Initial Report. We expect the report to be issued soon. If the CCWG final report recommends that some amount of the auction proceeds should be directed toward reserve replenishment then the IPC would support such a conclusion. \ ICANN’s current budget dilemma is not a sufficient reason to circumvent the CCWG’s multi-stakeholder process.

About the additional funds from contracted parties, we do not support a fee increase either one-time or permanent. It is our view that any increase would come at the expense of registrants. The entire global community should not be responsible for organizational mismanagement. The organization should be demonstrating fiscal restraint and making rational adjustments to expenses to offset the need to increase the reserve funds. A price increase should be the last resort not the first stop on the way to restoring ICANN’s fiscal health.

¹ See IPC Comments at <https://mm.icann.org/pipermail/comments-fy19-budget-19jan18/attachments/20180309/66ea6d71/IPCCommentsre2019OperatingPlanandBudget030818-0001.pdf>.

1.5 Guiding Principles – The IPC concurs with the guiding principles. We highlight ii. *“The ICANN org should make an annual contribution to the Reserve fund, without impairing its ability of carrying out its on-going operational activities in support of ICANN’s mission and the community”* and note that all sectors of the community will be affected by the necessary budget adjustments that ICANN will need to make to provide a minimum of \$3-5m USD per year to the reserves. (The IPC advises \$5m USD/year. ICANN has proposed \$3m USD/yr. See comments in 2.6 below.) We advise that when cuts are made, they are rational and proportional so that no single sector is adversely impacted more than another. Everyone will need to “feel the pain” to a certain degree. To the extent that ICANN org provides grants and assistance to third parties, ICANN should be looking at cutting support in measured ways over a few years rather than take a “slash and burn” approach that could cripple programs without giving them time to find additional sources of funding. This is particularly true for nonprofit organizations.

1.6 Replenishment Strategy – The IPC agrees that the replenishment should not exceed 5 years and should be accomplished sooner if feasible. The IPC disagrees with the proposed amount of ICANN org’s contribution from savings at \$3m USD/year and strongly recommends \$5m USD/yr. We note that this will entail larger organizational cuts and slow-to-no growth in expenses. Fiscal mismanagement got ICANN org where it is today and fiscal prudence will save it. Hard choices will have to be made but that is the core of proper business management and governance. Per our comments related to Sources of Funding above, IPC supports looking toward operational adjustments and left-over funds from the new gTLD program as the first sources for replenishment. Auction proceeds should not be considered unless the report from multistakeholder process currently underway recommends it. As a last resort, fees increases should be considered.

1.7 Assumptions – ICANN’s proposed replenishment strategy assumes that the reserve shortfall is unlikely to change given that operating expenses are likely to stabilize. IPC asks for more clarification for this assumption and whether ICANN is willing to commit to building more flexibility between projected revenues over projected expenditures This commitment would go a long way toward avoiding financial crises in the future.

3. Conclusion

The IPC is a very active participant in ICANN's policy making and governance. We take our role as a stakeholder seriously and welcome the opportunity to provide comments on critical ICANN operating procedures including the funding of ICANN's reserve fund. However, we note with much dismay that the state of the reserves is the result of a single-minded approach to the IANA transition "at any cost." This thinking and the actions stemming from it demonstrated poor management and poor governance and has placed ICANN in a vulnerable position both economically and politically. The consolation is that it is not too late to fix the problem and we are pleased to see ICANN org and the board owning the problem and taking the necessary steps to correct it. IPC looks forward to the Third Consultation Paper in later this year.

Respectfully submitted,

Intellectual Property Constituency