



June 15, 2012

Donuts Inc. offers these comments in reply to the gTLD Registries Stakeholder Group (RySG) Statement on the FY13 Draft Operating Plan & Budget – New TLD Fees, dated May 24, 2012. We agree with the RySG statement related to “excess funds” issues and offer some specific solutions.

ICANN’s draft budget related to New TLDs should be amended in two respects:

First, ICANN’s proposal to set up a policy development process (PDP) to determine what to do with excess application fees is procedurally flawed and violates the spirit and express statements ICANN made to new TLD applicants and to the community. That said, a distinction should be drawn between application fees and auction proceeds.

Second, the proposed New TLD budget for the 2,000 TLD scenario is embarrassingly padded beyond reason. It does not take into account efficiencies, economies of scale, or realism, especially in the case of risk assessment. We offer the attached alternative budget, which is conservative, but realistic in its assumptions. An artificially high budget in and of itself creates inefficiencies, over-spending, and incorrect incentives. The ICANN Board should not approve the proposed budget in its current form.

Refund Excess Application Fees

From the time of the GNSO council’s recommendation to approve the New TLD program to present—as embodied in the current draft budget—ICANN has clearly and repeatedly said the “New gTLD Application fee structure is based on the principles of cost recovery.” By its own repeated public statements, ICANN did not collect application fees to make a profit. Rather, the intent all along was for ICANN to cover its costs. If there are excess applications fees, they are owed to the applicants who paid the fees in the first place. It is as simple as that.

ICANN mistakenly suggests in its draft budget that staff may convene a PDP to determine what to do with excess application fees. ICANN staff is not empowered to convene a PDP, and, moreover, it should not be a community decision to return applicant funds. Overages from applicants are due in return to applicants, consistent with the nature of cost recovery and years of ICANN statements and

guidance. If ICANN did not set the \$185,000 application fee via a policy development process, it does not need one to determine disposition of excess fees.

As does the RySG, we distinguish between excess application fees and auction proceeds. ICANN absolutely should convene a community group to make recommendations for what to do with auction proceeds, which might be quite sizable considering the number of applicants for “top tier” names. That same community panel also should make recommendations regarding the almost \$30 million that ICANN has taken from application fees and allocated to repayment of historical costs of the New TLD program. The community should have input as to where that \$30 million is directed (e.g. reserve fund, return to registrants, foundation, etc.).

Reject Inflated New TLD Budget Proposal

ICANN should not approve the proposed New gTLD Application Processing Budget in the proposed 2,000 TLD application scenario. Total Operating Expenses of \$156.2 million and \$120 million for “risk” costs are grossly inflated.

It appears as if the 2,000 TLD budget is simply a 4x multiple of the 500 TLD scenario. In any budget assumption, efficiencies must be considered, as higher volume normally creates economies of scale (e.g., the first time takes longer and costs more than the hundredth time). For example, ICANN fails to account for the recurrence of applications from the same technical service providers: The five largest service providers account for approximately three-fourths of all applications. Similarly, many applicants have filed the same or similar applications. Indeed, for the most part, Donuts’ 307 applications utilize the same answers to virtually all questions. Thus, after the first few application evaluations, panelists will be able to evaluate subsequent applications much more efficiently for less time and costs.

In the proposed budget, ICANN allocates core ICANN staff operations too aggressively to the new gTLD budget. The allocation of \$7 million for ICANN staff equates to 20% of all of ICANN’s personnel costs. 10% seems more reasonable for an overhead allocation of ICANN staff costs.

Another overstated assumption is the proposed dramatic growth of the Quality Control (QC) line item. How could ICANN possibly spend \$8.6 million on QC (a sum more than ICANN’s total annual budget in 2004)? These costs should not be increased by a factor of four over the 500 TLD scenario. We recommend holding these costs to \$2 million, as documented in the 500 TLD budget. Any potential overages due to unanticipated events would be covered by the risk component of the budget.

As others have pointed out, the Independent Objector (IO) budget also is unreasonably high and, again, is merely a 4x multiple of the 500 TLD budget. A \$25 million IO is terribly inflated. It doesn’t make sense, creates the wrong incentive for

the IO, and sends the wrong message to the community. We suggest cutting the IO to the 1,000 TLD scenario, which would leave an ample budget of a still whopping \$12.5 million.

Finally, the risk cost component of the budget should not be increased based upon a straight-line to \$120 million. ICANN's risks associated with the new TLD program have lessened since the original \$30 million budget estimate was created, thanks to the passage of time and natural elimination of program risks (e.g., completion of vendor contracting, successful communication plan, completion of application window, and further clarification of the implementation plan). Moreover, there are efficiencies and economies of scale related to risk abatement and handling. A \$120 million war chest is preposterously high—in fact, it is larger than the GNP of several countries. We suggest that it be cut to 2x the original budget—a reasonable, and ample, \$60 million.

Donuts proposes the attached as a new TLD budget to amend the one posted on May 1, 2012. This budget still is based on conservative principles with plenty of contingency cushion. The revenue is based upon the actual number of applications, and expenses either match the ICANN staff proposal or are based upon a conservative doubling of the proposed 500 TLD budget. As such, it factors in the economies of scale and efficiencies clearly available to ICANN. Based on our estimates, ICANN will have collected approximately \$150 million in excess fees.

Timing of Refunds

With 1,930 applications, ICANN has collected fees of significant excess, and should refund a reasonable portion to applicants as soon as possible, preferably within the next 60 days. The initial refund should be at least \$20,000 per application, which represents just over 10% of the fees collected. After the program is completed, ICANN should do an accounting to determine the amount of the remaining portion of the refund.

Moreover, Donuts strongly encourages ICANN to comply with its own reporting commitments to ensure full accountability and prudent fiscal responsibility, especially when it pertains to such extensive financial resources. See ICANN's Cost Accounting Guidelines adopted in April 2010 (<http://www.icann.org/en/about/financials/cost-accounting-guidelines-22apr10-en.pdf>), which state (see page 10):

At least annually, cost reports are prepared more formally for the community. These reports include a report from an Independent Auditor...(and) includes information on the costs incurred, by organizational activity, for the fiscal year as well as inception-to-date costs incurred for specific programs such as for the new gTLD program. The annual cost report includes information related to forecasted costs-to-complete the program. The report also contains information on the exceptions noted in

cost accounting processes.

The absence of such measures would call into question the accountability of ICANN's budgeting and reporting process.

Conclusion

ICANN should refund excess application fees to applicants in a timely manner. While there may be good cause to establish a community group to make recommendations regarding auction proceeds and a \$30 million repayment of historical costs, there is no need for a community PDP to authorize a refund of excess application fees to applicants.

Applicant refund amounts should be based on a realistic New TLD budget. More importantly, the ICANN staff responsible for the New TLD budget should not be managing against an inflated budget. Applicant fees must be spent wisely and prudently. A realistic budget with regular auditing and reporting will ensure that occurs.

Sincerely,

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