

MOSSES ADAMS



**INTERNET CORPORATION FOR
ASSIGNED NAMES AND NUMBERS**

INDEPENDENT AUDITORS' REPORT

AND

FINANCIAL STATEMENTS

JUNE 30, 2008 and 2007

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors (Board)
The Internet Corporation for Assigned Names and Numbers

We have audited the accompanying statements of financial position of Internet Corporation for Assigned Names and Numbers (ICANN) as of June 30, 2008 and 2007, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the management of Internet Corporation for Assigned Names and Numbers. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Internet Corporation for Assigned Names and Numbers as of June 30, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Los Angeles, California
October 6, 2008

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

STATEMENTS OF FINANCIAL POSITION

JUNE 30, **2008** **2007**

Amounts are rounded to the nearest thousand in US Dollars

ASSETS

Cash and cash equivalents	\$ 22,005,000	\$ 31,031,000
Accounts receivable, net	12,456,000	14,970,000
Investments	24,773,000	-
Prepaid expenses	14,000	270,000
Other assets	404,000	97,000
Property and equipment, net	1,316,000	582,000
Total assets	<u>\$ 60,968,000</u>	<u>\$ 46,950,000</u>

LIABILITIES AND NET ASSETS

Liabilities		
Accounts payable and accrued liabilities	\$ 5,402,000	\$ 4,270,000
Deferred revenue	9,141,000	7,444,000
Total liabilities	<u>14,543,000</u>	<u>11,714,000</u>
Unrestricted net assets	<u>46,425,000</u>	<u>35,236,000</u>
Total liabilities and net assets	<u>\$ 60,968,000</u>	<u>\$ 46,950,000</u>

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

STATEMENTS OF ACTIVITIES

YEARS ENDED JUNE 30,

2008

2007

Amounts are rounded to the nearest thousand in US Dollars

UNRESTRICTED

SUPPORT AND REVENUE

Domain name registry and registrar fees	\$ 45,299,000	\$ 38,348,000
Address registry fees	823,000	823,000
Accreditation fees	3,667,000	3,597,000
Application fees	115,000	270,000
Interest income and other income	<u>829,000</u>	<u>433,000</u>
Total support and revenue	<u>50,733,000</u>	<u>43,471,000</u>

EXPENSES

Personnel	16,746,000	13,784,000
Travel and meetings	9,449,000	6,203,000
Professional services	8,854,000	5,864,000
Administration	4,957,000	3,219,000
Bad debt recovery	<u>(462,000)</u>	<u>(2,429,000)</u>
Total expenses	<u>39,544,000</u>	<u>26,641,000</u>
Change in net assets	<u>11,189,000</u>	<u>16,830,000</u>

UNRESTRICTED NET ASSETS

Beginning of year	<u>35,236,000</u>	<u>18,406,000</u>
End of year	<u>\$ 46,425,000</u>	<u>\$ 35,236,000</u>

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30,

2008

2007

Amounts are rounded to the nearest thousand in US Dollars

CASH FLOWS FROM OPERATING ACTIVITIES

Change in net assets	\$ 11,189,000	\$ 16,830,000
Adjustments to reconcile change in net assets to cash (used in) provided by operating activities:		
Depreciation expense	259,000	139,000
Bad debt recoveries	(462,000)	(2,429,000)
Unrealized loss	227,000	-
Changes in operating assets and liabilities		
Accounts receivable	2,976,000	975,000
Prepaid expenses	256,000	(48,000)
Other assets	(307,000)	(42,000)
Accounts payable and accrued liabilities	1,133,000	1,788,000
Deferred revenue	<u>1,697,000</u>	<u>2,490,000</u>
Net cash provided by operating activities	<u>16,968,000</u>	<u>19,703,000</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Purchases of property and equipment	(994,000)	(462,000)
Purchases of investments	<u>(25,000,000)</u>	<u>-</u>
Net cash used in investing activities	<u>(25,994,000)</u>	<u>(462,000)</u>

NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS

(9,026,000) 19,241,000

CASH & CASH EQUIVALENTS

Beginning of year	<u>31,031,000</u>	<u>11,790,000</u>
End of year	<u>\$ 22,005,000</u>	<u>\$ 31,031,000</u>

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - ORGANIZATION

The Internet Corporation for Assigned Names and Numbers (ICANN) was established in September 1998 under the laws of the state of California as a non-profit public benefit corporation. ICANN coordinates a select set of the Internet's technical management functions, such as the assignment of protocol parameters, the management of the domain name system, the allocation of Internet protocol (IP) address space, and the management of the root server system. Categories of Internet domains include Generic Top Level Domains (gTLDs) examples of which are *.com*, *.net*, *.org*, and *.edu* domains and Country Code Top Level Domains (ccTLDs), examples of which are *.us*, *.uk*, *.de*, and *.fr*. ICANN's primary sources of revenue are from domain name registration activities and DNS service providers as follows:

- **Domain name registry and registrar fees** for the registration and administration of Internet domain names. These fees include: 1) *Transaction fees from registrants of domain names via ICANN accredited registrars and gTLD registries* which are charged based upon a set rate per domain name registration, renewal, or transfer, and 2) *Fixed fees* which are amounts paid by registrars and registries in amounts set by contract for services rendered and/or rights given. ICANN also receives contributions and grants from other organizations.
- **Address registry fees** from organizations responsible for the assignment and administration of Internet addresses.
- **Accreditation fees** from ICANN accredited registrars for initial and annual renewal accreditation.
- **Application fees** from applicants seeking to become an ICANN accredited domain name registrar.

ICANN has three supporting organizations which serve as advisory bodies to the ICANN board of directors with respect to internet policy issues and structure within three specialized areas, including the system of IP addresses and the domain name system. The three supporting organizations are the Address Supporting Organization (ASO), Generic Names Supporting Organization (GNSO), and the Country Code Domain Name Supporting Organization (CCNSO). These supporting organizations are the primary source of substantive policy recommendations for matters lying within their respective specialized areas. The supporting organizations are not separately incorporated entities. Transactions handled by ICANN on behalf of GNSO are included in the accompanying financial statements.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation - The financial statements of ICANN have been prepared on the accrual basis of accounting. ICANN recognizes contributions, including unconditional promises to give, as revenue in the period received. Contributions and net assets are classified based on the existence or absence of donor-imposed restrictions. As such, the net assets of ICANN and the changes therein are classified and reported as follows:

- **Unrestricted net assets** - Net assets that are not subject to donor-imposed stipulations and that may be expendable for any purpose in performing the objectives of ICANN. ICANN's Board adopted an investment policy in November 2007. This investment policy established a Board designated Reserve Fund which limits use of the Reserve Fund based upon specific Board actions. All investments are designated under the Reserve Fund.
- **Temporarily restricted assets** - Net assets subject to donor-imposed stipulations that may or will be met either by actions of ICANN and/or the passage of time. As the restrictions are satisfied, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying financial statements as net assets released from restrictions.
- **Permanently restricted net assets** - Net assets subject to donor-imposed stipulations that resources be maintained in perpetuity. Investment income generated from these funds is available for general support of ICANN's programs and operations unless otherwise stipulated by the donor.

As of June 30, 2008 and 2007, ICANN had no permanently or temporarily restricted net assets.

Cash and cash equivalents - Cash and cash equivalents include deposits in bank, money market accounts, and marketable commercial paper. ICANN considers all cash and financial instruments with maturities of three months or less when purchased by ICANN to be cash and cash equivalents.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts receivable - ICANN carries its accounts receivable on invoiced amounts less allowances for doubtful accounts. On a periodic basis, ICANN evaluates its accounts receivable and establishes allowances based on overdue accounts and a history of past write-offs. ICANN had two major registries/registrar totaling approximately \$22,237,000 or 44% of total support and revenue in 2008 and one major registry/registrar totaling approximately \$14,394,000 or 34% of total support and revenue in 2007. ICANN had accounts receivable amounts totaling approximately \$3,881,000 and \$2,150,000 due from the major registries/registrar at June 31, 2008 and 2007, respectively.

ICANN recovered approximately \$462,000 and \$2,429,000 of bad debt expense during years ended June 30, 2008 and 2007, respectively.

Investments – Investments in marketable securities are carried at fair value, based on quoted market prices. In November 2007, the Board adopted an investment policy which established a Board designated Reserve Fund. All funds in investments are reserved by the Board as the Reserve Fund.

Property and equipment - Property and equipment are stated at cost or, for contributed items, at fair market value at date of contribution. The equipment, furniture and fixtures are being depreciated using the accelerated method over estimated useful lives of three to seven years. Leasehold improvements are being depreciated using the straight-line method over the useful life or the remaining lease term, whichever is shorter. Acquisitions of property and equipment in excess of \$10,000 are capitalized.

Deferred revenue – Revenue is recognized during the period that the transaction associated with a fee relates, regardless of when the transaction fee was billed. Unless a registrar elects to have their multi-year transaction fees billed on a deferred basis, all transaction years are billed during the quarter in which the transaction agreement was signed. Fees relating to future periods are recorded as deferred revenue until earned. Fees for which deferred billing has been elected are billed and recorded as revenues in the year the transactions associated with the fees occur.

Advertising costs - Advertising costs are expensed in the period incurred. Advertising expense amounted to approximately \$94,000 and \$16,000, for the years ended June 30, 2008 and 2007, respectively.

Income taxes - ICANN is exempt from federal and state income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code. Accordingly, no provision for income taxes has been made in the accompanying financial statements.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Functional allocation of expenses - Expenses that can be identified with a specific program or supporting service are charged directly to the related program or supporting service. Expenses that are associated with more than one program or supporting service are allocated based on methods determined by management. ICANN's expenses are classified approximately as follows for the fiscal years ended June 30:

	<u>2008</u>	<u>2007</u>
Program services	\$ 28,631,000	\$ 19,300,000
Support services: management and general	<u>10,913,000</u>	<u>7,341,000</u>
Total expenses	<u>\$ 39,544,000</u>	<u>\$ 26,641,000</u>

Concentration of credit risk - Financial instruments which potentially subject ICANN to concentrations of credit risk consist primarily of cash and cash equivalents, accounts receivable, and investments. ICANN places its cash with major and creditable financial institutions. The cash held at these financial institutions may, at times, exceed the amount insured by the Federal Deposit Insurance Corporation. Concentration of credit risk with respect to receivables is mitigated by the diversity of registries/registrar comprising ICANN's registry/registrar base. ICANN places its investments with a major and creditable investment broker. The investments held are subject to the volatility of the market and industry in which it is invested.

Use of estimates - The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications - Certain 2007 amounts have been reclassified in the financial statements to conform to the 2008 presentation. These reclassifications have no impact on net assets.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 3 - ACCOUNTS RECEIVABLE

Accounts receivable is comprised of the following as of June 30:

	<u>2008</u>	<u>2007</u>
gTLD registries and registrars	\$ 11,779,000	\$ 13,875,000
IP address registries	823,000	2,172,000
ccTLD's	451,000	232,000
Other	<u>3,000</u>	<u>12,000</u>
	13,056,000	16,291,000
Less: allowance for doubtful accounts	<u>(600,000)</u>	<u>(1,321,000)</u>
	<u>\$ 12,456,000</u>	<u>\$ 14,970,000</u>

NOTE 4 - INVESTMENTS

Investments consist of the following as of the year ended June 30, 2008:

Stocks	\$ 8,190,000
Bonds	<u>16,583,000</u>
Total	<u>\$ 24,773,000</u>

There were no investments for the year ended June 30, 2007.

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consists of the following at June 30:

	<u>2008</u>	<u>2007</u>
Computer equipment	\$ 1,453,000	\$ 752,000
Computer software	20,000	20,000
Furniture and fixtures	322,000	194,000
Leasehold improvements	<u>294,000</u>	<u>130,000</u>
	2,089,000	1,096,000
Less: accumulated depreciation	<u>(773,000)</u>	<u>(514,000)</u>
	<u>\$ 1,316,000</u>	<u>\$ 582,000</u>

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 6 - LEGAL MATTERS

In the ordinary course of business, ICANN is occasionally named as a defendant in lawsuits and may be involved in other alternative dispute resolution proceedings. Management is unable at this time to determine the probable outcome or the effect, if any, that these matters may have on the financial position and the ongoing operations of ICANN. Accordingly, the accompanying financial statements do not include a provision for any losses that may result from ICANN's current involvement in legal matters.

NOTE 7 - RELATED PARTY TRANSACTIONS

ICANN's President and Chief Executive Officer (CEO), Dr. Paul Twomey's services are currently provided to ICANN through a professional services agreement with Argo Pacific Party Limited (Argo Pacific), an Australian Proprietary Company. Dr. Twomey has an interest in Argo Pacific.

Payments were made to Argo Pacific under a contractual arrangement with ICANN (the terms of which have been approved by the ICANN Board of Directors) for the provision of Dr. Twomey's professional services, benefits allowance, and for related expenses (incidental travel, telecommunications, computer supplies, and office supplies).

Pursuant to the agreement, during the year ended June 30, 2008, Argo Pacific was paid \$256,000 associated with Dr. Twomey's employee benefits, \$543,000 in base compensation, and \$148,000 in bonuses. Argo Pacific's agreement with ICANN is denominated in Australian Dollars. ICANN's functional currency is in US Dollars, thus the payments to Argo Pacific are impacted by exchange rate fluctuations between the US dollar and Australian dollar. During the year ended June 30, 2007, Argo Pacific was paid \$219,000 associated with Dr. Twomey's employee benefits, \$451,000 in base compensation, and \$210,000 in bonuses. These bonuses were for service during the fiscal year ending June 30, 2004, 2005, and 2006. Furthermore, during the year ended June 30, 2007, Argo Pacific received \$24,000 in foreign currency adjustments for years prior to 2007 and received \$37,000 in foreign currency adjustments for the 2007 year. Reimbursements made to Argo Pacific for related expenses such as travel, telecommunications, and office supplies amounted to \$25,000 and \$26,000 for the years ending June 30, 2008 and 2007, respectively. Total payments made to Argo Pacific for the years ended June 30, 2008 and 2007, were approximately \$972,000, and \$967,000, respectively.

Included in accounts payable and accrued liabilities to Argo Pacific as of June 30, 2008 and 2007 was \$7,000 and \$143,000, respectively.

INTERNET CORPORATION FOR ASSIGNED NAMES AND NUMBERS

NOTES TO FINANCIAL STATEMENTS

NOTE 8 - COMMITMENTS

ICANN leases its offices and certain other facilities under operating lease agreements with termination clauses from three to twelve months. Rent expense amounted to approximately \$1,211,000 and \$535,000 for the years ended June 30, 2008 and 2007, respectively. Minimum payments under the cancelable operating leases for the future years ending June 30 are approximately:

2009	\$	1,189,000
2010		1,014,000
2011		823,000
2012		800,000
2013		<u>67,000</u>
Total	\$	<u>3,893,000</u>

ICANN has probable pass-through and additional charges from the sublessor which are not included in the minimum payments above. The pass-through and additional charges cannot be reasonably estimated for future periods. Pass-through and additional charges amounted to approximately \$494,000 and \$254,000 for the years ended June 30, 2008 and 2007, respectively.

NOTE 9 - DEFINED CONTRIBUTION PENSION PLAN

ICANN's 401(k) Plan (the "Plan") is available to all employees in the United States at the first of the month following hire date with ICANN. ICANN contributes 5% of employee's salary to the plan regardless of employee contributions. ICANN also matches employee contributions up to 10% of the employee's annual salary. Employer contributions for the years ended June 30, 2008 and 2007 amounted to approximately \$1,083,000 and \$709,000, respectively.