



February 2016

Dear Members

Review of the Nominet model

About a year ago the Board commissioned Sir Michael Lyons to undertake an independent external review of Nominet's operating model and governance arrangements. Sir Michael's report to the Board is being published today, together with the Board's response, actions taken so far, current status and expectations for the future.

As part of this process, Sir Michael met with Nominet's directors, some senior managers, a sample of Nominet members – intended to provide a representative cross-section of the whole membership, and wider stakeholders outside of the membership including from various government departments. He also attended the company Annual General Meeting in June, and offered to speak with any other member not already involved in the review process. The final report was presented to Nominet's board in November 2015 and since then we have taken time as a Board to fully absorb his report and to consider our response to Sir Michael's recommendations.

On behalf of my Board colleagues I want to thank Sir Michael for getting to grips with Nominet's complicated ecosystem, and for producing such a thorough and thoughtful analysis of our issues. I hope all will agree that he has done a good job and provided his views on some of the challenges that face us. The report reflects the achievements and successes of the company over the years, and in particular the commercial success of the .UK ccTLD, and some of the tensions which this has led to. Although this has not made the Board's job easy at times, we are proud of this success and relish the opportunities that the internet provides for the future.

Since the Board started this project we have of course welcomed our new Chief Executive, Russell Haworth. David Thornton was elected to the Board as a non-executive director, and we also have appointed Andrew Pinder in the place of Clive Grace, and Jane Tozer who was appointed on an interim basis to fill the vacancy created when Oliver Hope joined Nominet as a full time employee. We have also been progressing our business plan and that has included looking more closely at some of our governance arrangements. Naturally some of this work has overlapped with Sir Michael's review. Where we have not totally accepted a recommendation or there is overlap with existing work, we have set that out in order to explain our thinking.

Over the course of my last year as Chair of Nominet, I look forward to updating members on our progress towards completion of the actions to be taken against those recommendations marked as 'ongoing' in the attached schedule.

Yours sincerely

Rennie Fritchie
Chair, Nominet UK

Sir Michael's recommendations

In total there are 19 recommendations. In assessing our response, the Board felt that these could usefully be divided into the following three categories:

- A. Firstly, general recommendations about Nominet's Public Purposes, role and governance arrangements;
- B. Secondly, three recommendations specifically on the topic of diversification; and
- C. Finally, recommendations covering membership, and the relationship between the company and its members, and stakeholder involvement wider than simply the membership.

A. Nominet's Public Purposes, role and governance arrangements

Recommendation 2: Nominet should define and agree its public purposes

Nominet Response:

We agree with the recommendation, which builds on considerable work already undertaken in 2015 to restate the way in which we express our commitment to working for the public benefit. The Executive provided an update at our January meeting, and a full proposal is due at the March Board meeting. Following this will begin the process of explaining to members and wider stakeholders how we will apply these principles in practice.

Status: ongoing

Recommendation 7: Nominet should clarify its own view of its regulatory responsibilities and ensure this is carefully and consistently reflected in all future public statements

Nominet Response:

The Board accepts this recommendation.

Sir Michael's view is that Nominet clearly is not a regulator; the industry regulator is OFCOM. We agree with that clarification, and take on board Sir Michael's comments that terminology should be consistent with that understanding in future.

Status: complete and closed

Recommendation 10: Nominet should review the structure of the board's working parties and sub-committees with a view to reducing its complexity.

Nominet Response:

We accept this recommendation in principle, recognising that a simple structure with minimal duplication of effort is desirable. Our overriding aim is for the most effective decision and oversight structure for the company, and this will involve delegation of matters between Board meetings to groups of one or more directors from time to time.

Whilst some formal committee structure is also necessary for compliance with best practices in UK corporate governance, we have reduced the number of Board working groups. The Development Working Group and International Working Group have been disbanded, and the activities of the Model Review Working Group will end with this document. Member Engagement will in future be a whole Board initiative. As members will know, Nominet Registrar Services Limited, our ICANN accredited registrar subsidiary, is being mothballed until further notice and therefore we do not anticipate much Board resource being expended on it. The Member Code of Conduct Committee is only convened on an ad hoc basis in the event of a complaint being raised with us that a Nominet member is acting in such a way which is bringing the company into disrepute, and its proceedings have so far been very limited.

This leaves the four formal Board committees: Audit and Governance, Investment, Remuneration and Nominations, together with the Elections Sub-Committee of the Nominations Committee which is convened each year. We believe that this is now an appropriate structure for the Board to discharge its responsibilities and to carry out its programme of work.

Status: complete and closed

Recommendation 12: Nominet should define board positions in terms of the skills needed.

Nominet Response:

We accept this recommendation.

Whilst operating a unitary Board structure, and therefore each director having the same legal duties towards the company, we have essentially three different categories of director, depending on their appointment process, and whether they have executive responsibilities.

Firstly the independent non-executive directors, who are all appointed (subject to member approval at general meeting) on the basis of open advertisement and competitive selection by interview and assessment of skills and experience for the position requirements. These positions therefore already have a defined set of skills requirements.

Secondly our executive directors, who are all permanent members of staff with service contracts, including a job description and fully defined skills and competencies expected of the role holder.

Finally we have non-executive directors who are elected by our members. Whilst the appointment decision is made by the members, these roles again have defined skills and competencies sought in the ideal candidate and which are set out in the call for nominations pack.

Status: complete and closed

Recommendation 13: The Board should consider stepping back from being so closely involved in issuing advice on preferred candidates but should, instead, be clear about the characteristics and skills that it needs for the future of the company and invite all candidates to indicate how they measure up against those skills.

Nominet response:

This is an area where there have been numerous Board discussion and debate over the years. Whilst in general the Nominet Board agrees that the default position is not to state a preference as between validly nominated election candidates, in practice it would be difficult to accept this recommendation in its entirety.

Firstly we should point out that we have been very clear in recent years as to the range of skills that would be ideally found in the successful election candidate(s). Nominees are required to provide a description as to why they feel they should be elected by members, together with a CV and statement of interests. Ultimately, however, the decision is for members to make, regardless of whether or not the Board feels that some candidates better meet the published job specification. In that sense, we believe we already operate our elections in accordance with the spirit of this recommendation.

Where the Board becomes aware of a material non-disclosure or other statement of fact which the Board feels is misleading to members, we do not feel that in all conscience we can accept this recommendation entirely. In our view, the Nominet Board should always be able (if not obliged) to put the record straight in order that members have a full and fair picture upon which to base their voting decisions.

Status: complete and closed

Recommendation 14: The Board should not now seek to make changes to the current pattern of non-executive directors but instead strengthen the skills around the table for sub-committees and subsidiary companies.

Nominet response:

The Board accepts this recommendation.

The pattern of non-executive directors is set out in the company's articles of association, and is therefore ultimately a decision for members to make. The current Board structure is felt to be working well, and in line with best practice we have an annual review of Board effectiveness where this position is reassessed on a regular basis. There will be no proposal from the Board for any change in pattern of non-executive directors in 2016. In future years this assessment may change depending on the needs of the company at that time.

The Board also accepts that there may be a need for specific skills sets which are not present or available from time to time, and that we should not be constrained by the make up of the Board in order to seek out additional expertise.

Status: complete and closed

Recommendation 15: The Board should consider the addition of an executive finance director to the main board.

Nominet Response:

The Board has considered this recommendation, and noted that there is a vacant position for an additional executive director to be appointed to the Board. The Board further notes and understands that an executive finance director is a common role to be found on a company's board of directors and, indeed, that Nominet has in the past piloted such a role. However on balance the non-executive directors do not currently feel that there is a need for such a role to be created. Whilst Nominet is a commercial company, its operations are not complex financially. Nor is the company concerned with driving total shareholder return, as a typical dividend generating enterprise would be. The company has a recently appointed Director of Finance which whilst not a Board appointment reports directly to the Chief Operating Officer and also attends Board meetings for discussion of finance matters.

The structure of the finance department will (as any other part of the company) be subject to review from time to time, and in the future it may be appropriate to have a finance director on the main board in order to meet the future needs of the business.

Status: complete and closed

Recommendation 16: Actively plan board succession so that term extensions are not required

Nominet response:

The Board accepts this recommendation.

The directors are not subject to a specific term limit, but there is an expectation that our appointed non-executive directors generally will not serve on the Board for longer than six years. The Board recognises that the introduction of three new appointed non-executive directors in 2010 all starting at the same time has meant that there has been a 'bunching' effect and ideally appointments would be staggered for better continuity.

Going forwards, Piers White is retiring at the 2016 AGM upon completion of a six year term and Rennie Fritchie has a one year extension to the 2017 AGM to ensure some continuity as our recent appointments complete their first year in post. After this, we do not consider that any further extensions will be necessary at this time.

Status: complete and closed

Recommendation 19: The Board should consider the current balance of executive representation on the Board

Nominet response:

The Board have considered the balance of executive representation, currently constituting three members out of a total of ten. There are seven non-executive directors, three of whom are appointed (and therefore independent of membership and other conflicts of interest as registrars) and four are elected by the membership. We therefore believe that we have a balanced set of skills and interests around the boardroom table. In addition, whilst we are not a company admitted to the stock exchange, this would comfortably meet the requirements of the UK Corporate Governance Code for smaller listed companies to have at least two non-executive directors independent of membership interests.

Status: complete and closed

Recommendation 17: Nominet should adopt the key principle of "comply or explain" as regards the UK Corporate Governance Code

Nominet response:

The Board accepts this recommendation.

The UK Corporate Governance Code applies to all companies with a premium listing of equity shares on the London Stock Exchange and hence is not a legal requirement for Nominet. Further, as company limited by guarantee and with members as opposed to shareholders, there are whole sections are not relevant to Nominet. However we agree that the UK Corporate Governance Code is considered to reflect best practices, and that Nominet should comply with it in terms of governance procedures such as executive appointment

and remuneration. In accordance with the Code itself, where we do not comply then the reasons for non-compliance should be set out in our Annual Report.

The Board and each of its Committees has already completed a process of reviewing all the provisions of the UK Corporate Governance Code in order to identify any areas in which the comply or explain principle requires further work. This is in the process of being implemented in the preparation of the 2015 Annual Report.

Status: ongoing

Recommendation 9: Nominet should continue to play an active part in national and international debate about the future of the internet and especially any steps to bring in new regulation

Nominet response:

The Board agrees with this recommendation.

Nominet has played a full part in many national and international internet governance debates and policy development, including at ICANN and at home within the UK's parliamentarians and regulators. We see this fully within our remit going forwards.

Status: complete and closed

B. Diversification

Recommendation 3: Consider the introduction of a competitive impact test as regards the introduction of new products and services, particularly focused on the impact upon members

Nominet response:

The Board accepts this recommendation.

In making decisions as to the most appropriate strategic diversification opportunities for the company to pursue, we have always taken into account the likely response from our members, and whether an opportunity for Nominet would be viewed as a threat or a mutual opportunity for benefit. However we accept that this process has been ad hoc and not applied consistently or rigorously.

We have therefore asked the executive to identify some options for an appropriate competitive impact test, to be presented to the Board in the first half of 2016.

Status: ongoing

Recommendation 11: The board may wish to consider whether any immediate steps would help to further demonstrate its commitment to the protection and enhancement of the ccTLD registry function and to ring-fence the financial risks involved in diversification

Nominet response:

The Board accepts this recommendation.

It is disappointing that the central importance to Nominet of the protection and enhancement of our core registry service is not felt to be sufficiently well articulated at present. The vast majority of our staff time and annual expenditure is focussed on the .UK ccTLD, and the safe and secure operation of the .UK ccTLD is a central feature of our corporate objectives against which the Board assess the executive each year. Any significant negative deterioration in the technical service provision or financial security of the .UK ccTLD would breach these objectives. The .UK ccTLD is also the main focus of the company Risk Register which is regularly reviewed by the Audit and Governance Committee.

We will therefore publish the corporate objectives for 2015-16 in order to demonstrate this commitment. Going forwards as our plans for diversification progress, the Audit and Governance Committee will monitor closely any risks posed to the security of the core .UK ccTLD, and we will provide updates in due course.

Status: ongoing

Recommendation 18: Nominet should make public the KPIs by which it holds the executive to account reflecting at the minimum registry costs and progress with diversification

Nominet response:

The Board accepts this recommendation.

An update will be provided in due course.

Status: ongoing

C. Membership, the relationship between the company and its members, and stakeholder involvement wider than simply the membership

Recommendation 1: The Nominet Board need to extend efforts to effectively engage with the membership. A key part of this is the development of a strong, clear narrative for the membership about the company's future

Nominet response:

The Board accepts this recommendation.

In the Annual Report for 2014-15 we set out for members an overview of the company, including the historical background and challenges we face as the core domain name business becomes subject to new competitive pressures. However we accept that we have struggled with effective membership engagement, and recognise that more effort needs to be extended in this area.

Status: ongoing

Recommendation 4: The company should discuss with its membership the most appropriate channels for future communication between the board and the membership

Nominet response:

The Board accepts this recommendation.

Sir Michael spent considerable time with both Board members and those members of Nominet who would probably consider themselves to be the most engaged. The clear implication here is that the current system of formal reports following each Board meeting, email 'Nom-Announces' to all members and the events that we put on for members each year are not working well enough.

Status: ongoing

Recommendation 6: The company should strengthen relationships with other stakeholders, including a wide range of voices representing different end users and organisations interested in the future development of the internet and digital economy. The results of this dialogue should be shared with members.

Nominet response:

The Board accepts this recommendation.

We recognise that there are certain sectors of internet users, small businesses and individuals in particular, that we should engage more with. We are therefore going to review our non-member, non-government stakeholder engagement, in order to better capture the views of wider civil society in areas of internet development and the digital economy. We will provide an update in due course.

Status: ongoing

Recommendation 8: Nominet should establish separate, more open, arrangements for consultation and dialogue with Government and find ways of reporting conclusions emerging from those discussions to the membership

Nominet response:

The Board accepts this recommendation and will discuss with Government ways in which this recommendation can be taken forward.

Although the Department for Culture, Media and Sport (DCMS) are represented on the .UK stakeholder committee, Sir Michael clearly recommends a more structured approach which is distinct from other stakeholder relationships.

Status: ongoing

Recommendation 5: Nominet should reconsider the link between membership and discounted domain registration fees

Nominet response:

As prompted by this recommendation, the Board have reconsidered whether discounted domain registration fees should only be available to members of Nominet. Since Nominet's foundation our constitution has required that voting rights are determined in accordance with each member's relative commercial involvement in the .UK namespace. The requirements to be admitted as a member of Nominet were intentionally kept to a minimum, together with a low membership fee. The combined effect was to ensure a wide and inclusive a membership as possible, and to draw into Nominet's membership structure and governance all participants in the .UK namespace. We believe that this continues to provide a reasonably stable structure for the company and adds legitimacy to our role as the national registry.

For the time being, we are therefore not going to review the link between membership and discounted domain registration fees.

Status: complete and closed