

American Registry For Internet Numbers, Ltd.

Financial Report
December 31, 2012

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Independent Auditor's Report

To the Board of Trustees
American Registry for Internet Numbers, Ltd.
Chantilly, Virginia

Report on the Financial Statements

We have audited the accompanying financial statements of American Registry for Internet Numbers, Ltd. (ARIN) which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ARIN as of December 31, 2012 and 2011, and the change in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

The image shows a handwritten signature in black ink that reads "McGladrey LLP". The signature is written in a cursive, flowing style.

Gaithersburg, Maryland
April 22, 2013

American Registry For Internet Numbers, Ltd.

Statements Of Financial Position
December 31, 2012 And 2011

Assets	2012	2011
Cash And Cash Equivalents	\$ 1,201,441	\$ 1,422,905
Investments		
Legal Defense Reserve Fund	2,089,541	2,084,554
Operating Reserve Fund	3,588,560	2,832,655
Long-Term Reserve Fund	21,282,950	19,384,291
	<u>26,961,051</u>	<u>24,301,500</u>
Accounts Receivable, net	331,102	278,725
Prepaid Expenses	439,491	426,206
Note Receivable	-	90,000
Property And Equipment, net	4,705,834	4,553,831
Software Costs	143,992	540,120
Deposits	73,659	236,189
	<u>\$ 33,856,570</u>	<u>\$ 31,849,476</u>
 Liabilities And Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 1,159,149	\$ 1,402,981
Due to ICANN	130,000	89,553
Due to NRO	28,682	-
Deferred rent	44,167	24,242
Deferred revenue	5,663,137	5,676,792
Total liabilities	<u>7,025,135</u>	<u>7,193,568</u>
Commitments (Note 7)		
Net Assets		
Unrestricted	26,831,435	24,655,908
	<u>\$ 33,856,570</u>	<u>\$ 31,849,476</u>

See Notes To Financial Statements.

American Registry For Internet Numbers, Ltd.

Statements Of Activities
Years Ended December 31, 2012 And 2011

	2012	2011
Revenue and support:		
Registration	\$ 12,189,843	\$ 11,496,281
IP end-user registrations	1,277,750	1,415,250
Maintenance fees	1,131,600	1,160,500
Contributions	296,975	209,850
Network transfers	68,500	57,250
Membership dues	19,500	22,000
Other revenue	7,324	5,524
Total revenue and support	14,991,492	14,366,655
Operating expenses:		
Program services:		
Engineering	6,862,301	6,664,935
Member services	3,344,107	2,978,688
Registration services group	2,643,050	2,490,933
Outreach services	-	343,150
Total program services	12,849,458	12,477,706
Support services:		
General and administrative	2,702,056	2,584,372
Total operating expenses	15,551,514	15,062,078
Change in net assets before investment activities	(560,022)	(695,423)
Interest and dividends	632,804	661,740
Realized and unrealized gains (losses) on investments	2,102,745	(1,016,951)
Change in net assets	2,175,527	(1,050,634)
Unrestricted net assets, beginning of year	24,655,908	25,706,542
Unrestricted net assets, end of year	\$ 26,831,435	\$ 24,655,908

See Notes To Financial Statements.

American Registry For Internet Numbers, Ltd.

Statements Of Cash Flows
Years Ended December 31, 2012 And 2011

	2012	2011
Cash Flows From Operating Activities		
Change in net assets	\$ 2,175,527	\$ (1,050,634)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,794,733	1,619,577
Realized and unrealized (gains) losses in investments	(2,102,745)	1,016,951
Loss on disposal of property and equipment	161,919	2,080
Bad debt expense	94,126	38,889
Changes in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	(146,503)	(70,621)
Prepaid expenses	(13,285)	28,991
Software costs	238,371	177,189
Deposits	162,530	(125,749)
Increase (decrease) in:		
Accounts payable and accrued expenses	(243,832)	64,305
Due to ICANN	40,447	(12,169)
Due to NRO	28,682	-
Deferred rent	19,925	(12,014)
Deferred revenue	(13,655)	598,219
Net cash provided by operating activities	2,196,240	2,275,014
Cash Flows From Investing Activities		
Property and equipment acquisitions	(1,950,898)	(2,702,803)
Proceeds from the sale of investments	824,863	5,448,144
Purchase of investments	(1,381,669)	(4,531,582)
Advance made under note receivable	-	(60,000)
Collections on note receivable	90,000	-
Net cash used in investing activities	(2,417,704)	(1,846,241)
Net (decrease) increase in cash and cash equivalents	(221,464)	428,773
Cash And Cash Equivalents:		
Beginning	1,422,905	994,132
Ending	\$ 1,201,441	\$ 1,422,905

See Notes To Financial Statements.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 1. Nature Of Activities And Significant Accounting Policies

Nature of activities: American Registry for Internet Numbers, Ltd. (ARIN) was established on August 28, 1997, and began operations on December 22, 1997. ARIN provides services related to the technical coordination and management of Internet number resources in its service region which is Canada, the United States and several islands in the Caribbean Sea and North Atlantic Ocean. ARIN facilitates the development of consensus-based policies made by its members and stakeholders, and provides information and educational outreach.

Basis of accounting: The accompanying financial statements are presented in accordance with the accrual basis of accounting.

Basis of presentation: The accompanying financial statement presentation follows the recommendations under the Not-for-Profit Entities Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). ARIN reports information regarding its financial position and activities according to the existence or absence of externally (donor) imposed restrictions into three classes of net assets. The net asset classes are: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets. ARIN had no temporarily or permanently restricted net assets at December 31, 2012 and 2011.

The Board of Trustees has designated net assets for the following purposes:

Legal Defense Reserve Fund: To fund legal challenges as they arise. At December 31, 2012 and 2011, the Legal Defense Reserve Fund totaled \$2,089,541 and \$2,084,554, respectively.

Operating Reserve Fund: To provide short-term financial stability for ARIN. The Operating Reserve Fund totaled \$3,588,560 and \$2,832,655 at December 31, 2012 and 2011, respectively.

Long-Term Reserve Fund: To provide long-term financial stability for ARIN. At December 31, 2012 and 2011, the Long-Term Reserve Fund totaled \$21,282,950 and \$19,384,291, respectively.

Cash and cash equivalents: For the purposes of the statements of cash flows, ARIN considers all highly liquid instruments purchased with an original maturity of three months or less and available for general operating purposes to be cash equivalents. Cash accounts maintained in brokerage accounts are subject to Board of Trustees' approval and are not considered as cash and cash equivalents.

Financial risk: ARIN maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. ARIN has not experienced any losses in such accounts and believes it is not exposed to any significant financial risk on cash.

ARIN invests in a portfolio that contains certificates of deposit, exchange traded funds and mutual funds. Such investments are exposed to various risks, such as market and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term could materially affect investment balances and the amounts reported in the financial statements.

Investments: ARIN includes in investments all accounts, including money market funds, which are managed by investment advisors. Investments are recorded at fair market value, and realized and unrealized gains and losses are reported in the accompanying statements of activities.

Accounts receivable: Accounts receivable are recorded at original invoice less an estimate made for doubtful receivables and consist principally of registration fees. ARIN uses the allowance method to determine uncollectible accounts receivable. Management establishes an allowance for all outstanding receivables aged over 90 days. At December 31, 2012 and 2011, management established an allowance in the amount of \$58,078 and \$53,500, respectively.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 1. Nature Of Activities And Significant Accounting Policies (Continued)

Property and equipment: ARIN capitalizes all property and equipment purchased of \$1,000 or more at cost. Expenditures for additions, renewals, and improvements are capitalized; expenditures for maintenance and repairs are charged to expense as incurred. Upon disposal of property, the cost and accumulated depreciation are eliminated from the accounts and any resulting gain or loss is included in operations.

Leasehold improvements are amortized over the ten-year term of the lease. Depreciation of property and equipment is provided for using the straight-line method over the estimated useful life of the assets which range from three to five years.

Software costs: ARIN expenses preliminary project stage costs as incurred. Capitalized applications stage costs are amortized over five years using the straight-line method. Post-implementation and operation stage costs are expensed as incurred.

Impairment of long-lived assets: ARIN accounts for the valuation of long-lived assets under ASC 360, *Accounting for the Impairment or Disposal of Long-Lived Assets*. ASC 360 requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell. As of December 31, 2012 and 2011, management has determined that there has been no impairment in the carrying value of long-lived assets reflected in the accompanying financial statements.

Deferred revenue: Revenue received in advance of the period in which it is earned is deferred to subsequent periods. Deferred revenue is comprised principally of registration fees received in advance.

Income taxes: ARIN is a qualifying not-for-profit organization as defined in Section 501(c)(6) of the Internal Revenue Code and is exempt from federal income taxes. Accordingly, no provision for income taxes has been made in the accompanying financial statements.

The accounting standard for uncertainty in income taxes, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return, should be recorded in the financial statements. Under this guidance, ARIN recognizes the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes, and accounting in interim periods.

Management evaluated ARIN's tax positions and concluded that ARIN had taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance. Generally, ARIN is no longer subject to income tax examinations by the U.S. federal, state or local tax authorities for years before 2009.

Revenue recognition: Registration revenue of ASN registrations and IP initial registrations are recognized in the applicable period. Resources are not issued until payment is received.

Both initial and renewal registration revenue are recognized in the corresponding period in which the services are rendered.

Membership dues are recorded as revenue in the applicable period to which the membership applies.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 1. Nature Of Activities And Significant Accounting Policies (Continued)

Use of estimates: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Such estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Functional allocation of expenses: The costs of providing various programs and other activities have been summarized on a functional basis in the statements of activities. Expenses are charged to each program based on direct expenditures incurred. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Certain management and staff expenses have been allocated to programs on a percentage basis.

Reclassifications: Certain items in the December 31, 2011, financial statements have been reclassified to conform to the December 31, 2012, financial statement presentation. These reclassifications had no effect on the previously reported change in net assets.

Subsequent events: In preparing these financial statements, ARIN has evaluated subsequent events through April 22, 2013, which is the date the financial statements were available to be issued.

Note 2. Investments And Fair Value Measurements

In accordance with the FASB Codification statement, *Fair Value Measurements*, ARIN has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy.

The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument. Investments recorded in the statements of financial position are categorized based on the inputs to valuation techniques as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. The types of investments included in Level 1 include listed equities and mutual funds.

Level 2 – Inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly, and fair value is determined through the use of models or other valuation methodologies. Investments which are generally included in this category include corporate loans, less liquid, restricted equity securities and certain corporate bonds, government obligations and over-the-counter derivatives.

Level 3 – These are investments where values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect assumptions of management about assumptions market participants would use in pricing the investments. These investments include non-readily marketable securities that do not have an active market.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 2. Investments And Fair Value Measurements (Continued)

Exchange traded and mutual funds: Valued at quoted market prices in active markets for identical assets.

Certificates of deposit: Valued at market prices based upon observable inputs such as interest rates.

The following table sets forth by level, within the fair value hierarchy, ARIN's assets at fair value at December 31, 2012 and 2011.

	December 31, 2012			
	Level 1	Level 2	Level 3	Total
Equity exchange traded funds	\$ 2,575,938	\$ -	\$ -	\$ 2,575,938
Taxable bond exchange traded fund	1,584,185	-	-	1,584,185
Mutual funds, balanced funds				
Bond fund	5,747,235	-	-	5,747,235
Blended funds	5,471,844	-	-	5,471,844
Growth funds	4,444,906	-	-	4,444,906
Commodities broad basket funds	848,735	-	-	848,735
Foreign blended funds	569,723	-	-	569,723
	17,082,443	-	-	17,082,443
Certificates of deposit	-	481,184	-	481,184
	\$ 21,242,566	\$ 481,184	\$ -	\$ 21,723,750
	December 31, 2011			
	Level 1	Level 2	Level 3	Total
Equity exchange traded funds	\$ 2,345,617	\$ -	\$ -	\$ 2,345,617
Taxable bond exchange traded fund	1,547,727	-	-	1,547,727
Mutual funds, balanced funds				
Bond fund	5,147,703	-	-	5,147,703
Growth funds	4,265,258	-	-	4,265,258
Blended funds	4,189,759	-	-	4,189,759
Foreign blended funds	1,059,188	-	-	1,059,188
Commodities broad basket funds	806,508	-	-	806,508
	15,468,416	-	-	15,468,416
Certificates of deposit	-	2,248,383	-	2,248,383
	\$ 19,361,760	\$ 2,248,383	\$ -	\$ 21,610,143

Money market funds of \$5,237,301 and \$2,691,357 as of December 31, 2012 and 2011, respectively, are not included in the total investments as they are carried at cost.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 3. Note Receivable

In October 2010, ARIN executed a loan agreement of up to \$180,000 with NewNOG, Inc. under commercial terms to provide for Executive Director services during its early formation period. The agreement provided advances to NewNog of up to \$30,000 on a quarterly basis through January 1, 2012. Interest accrued on the outstanding balance at an annual rate of 2%. Repayments of the loan commenced on October 1, 2012, in equal quarterly principal and interest payments pursuant to a 25-month amortization schedule. Full payment of the outstanding balance was due by January 1, 2014. The note, however, was repaid in full during the year ended December 31, 2012.

Note 4. Property And Equipment

Property and equipment and accumulated depreciation at December 31, 2012 and 2011, are as follows:

	2012	2011
Database	\$ 6,046,572	\$ 4,461,552
Computer equipment	3,478,156	3,771,844
Computer software	694,878	649,630
Furniture and fixtures	315,766	322,018
Office equipment	101,423	103,361
Leasehold improvements	751,017	751,017
	<u>11,387,812</u>	10,059,422
Less accumulated depreciation and amortization	<u>(6,681,978)</u>	(5,505,591)
	<u>\$ 4,705,834</u>	<u>\$ 4,553,831</u>

Note 5. Retirement Plan

ARIN has a 401(k) retirement plan which is available to all employees within their first month of hire. ARIN makes a discretionary matching contribution equal to 200% of the first 3% of salary deferred and 100% of the next 3% deferred. Total retirement plan expense for 2012 and 2011 was \$706,825 and \$545,694, respectively.

Note 6. Related Party Transactions

On October 24, 2003, the four Regional Internet Registries (RIRs) and ARIN, along with Asia Pacific Registry (APNIC), Latin American Registry (LACNIC) and European Registry (RIPE NCC), entered into a memorandum of understanding to form the Number Resource Organization (NRO). In April 2005, ICANN recognized the African Registry (AfriNIC) as the fifth RIR in the world. Until 2004, number resources were managed in Africa by the RIPE NCC, ARIN, and APNIC.

The purpose of the NRO is to undertake joint activities of the Regional Internet Registries (RIRs), including joint technical projects, liaison activities and policy coordination. The NRO Executive Council consists of one person selected by each RIR. NRO expenses are borne by the RIR signatories on an equal basis of each RIR, unless specifically superseded by a specific or general per capita agreement by the NRO Executive Council. RIRs may donate funds, personnel, services and equipment to the NRO at their individual discretion in addition to the provisions for cost sharing. ARIN's contribution to finance the operations of NRO for 2012 and 2011 were \$50,153 and \$80,068, respectively.

ARIN is provided internet numbers for distribution by the Internet Corporation for Assigned Names and Numbers (ICANN). ARIN pays ICANN a voluntary contribution based on ARIN's fees collected and resources allocated. During 2012 and 2011 ARIN paid ICANN \$183,444 and \$166,937, respectively.

American Registry For Internet Numbers, Ltd.

Notes To Financial Statements

Note 7. Commitments

Lease commitments: During 2011, ARIN amended their lease for office space in Chantilly, Virginia. ARIN occupies the space under an operating lease expiring in January 2019, with a current base monthly rental payment of \$20,349. The base rent is subject to an annual escalation percentage of 3% and increases in its proportionate share of operating expense. Deferred rent is recorded in relation to the escalating lease payments.

Future minimum lease payments for the years ending December 31 are as follows:

<u>Years Ending December 31,</u>	
2013	\$ 250,899
2014	258,426
2015	266,179
2016	274,164
2017	282,389
2018 – 2019	315,158
	<u>\$ 1,647,215</u>

Rent expense totaled \$263,516 and \$227,422 during 2012 and 2011, respectively.

Severance agreement commitments: ARIN provides various severance plans to employees within various levels of the organization and for various time periods up to 12 months.



Independent Auditor's Report On The Supplementary Information

To the Board of Trustees
American Registry for Internet Numbers, Ltd.
Chantilly, Virginia

We have audited the financial statements of American Registry for Internet Numbers, Ltd. (ARIN) as of and for the years ended December 31, 2012 and 2011, and have issued our report thereon which contains an unmodified opinion on those financial statements. See pages 1 – 2. Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

McGladrey LLP

Gaithersburg, Maryland
April 22, 2013

American Registry For Internet Numbers, Ltd.

Schedules Of Operating Expenses
Years Ended December 31, 2012 And 2011

	2012	2011
Salaries and employee benefits	\$ 7,759,653	\$ 7,177,849
Hiring costs	28,465	50,299
Personnel	7,788,118	7,228,148
Depreciation and amortization	1,794,733	1,619,577
Communications	679,461	881,280
Equipment support and licenses	480,181	464,547
Operations	2,954,375	2,965,404
Travel	1,005,456	1,122,513
Legal expense	738,449	1,029,916
General office	893,216	654,058
Members meeting	437,850	408,394
Rent and occupancy	405,492	378,358
Consulting expense	327,679	369,440
Outreach expense	374,775	232,954
Contingency expense	3,761	47,404
General office and administrative	4,186,678	4,243,037
ASO support and AC support	187,099	217,901
ICANN support	183,444	166,937
Internet research and support	201,647	160,583
NRO	50,153	80,068
Internet support	622,343	625,489
	\$ 15,551,514	\$ 15,062,078