

ITEM FOR FINANCE COMMITTEE

LOAN FUND

NEW HEAD “INFORMATION TECHNOLOGY”

New Subhead “Loan to Hong Kong Internet Registration Corporation Limited”

Members are invited to approve the creation of -

- (a) a new Head “Information Technology” under the Loan Fund; and
- (b) a new Subhead “Loan to Hong Kong Internet Registration Corporation Limited” under the new Head, with a commitment of \$6.5 million to provide a loan to the newly established Hong Kong Internet Registration Corporation Limited.

PROBLEM

The Hong Kong Internet Registration Corporation Limited (HKIRCL) is newly established to administer Internet domain names in Hong Kong. It is unable to secure sufficient funds to start and maintain its operations in the initial years.

PROPOSAL

2. The Secretary for Information Technology and Broadcasting proposes to create a new Head “Information Technology” under the Loan Fund and, under the new Head, a new Subhead “Loan to Hong Kong Internet Registration Corporation Limited” with a commitment of \$6.5 million. The loan will enable HKIRCL to start and maintain its operations in the initial years.

/JUSTIFICATION

JUSTIFICATION

Administration of Internet domain names in Hong Kong

3. The administration of Internet domain names is a key element of the information infrastructure necessary for developing Hong Kong into a leading digital city. We must ensure that the administration of Internet domain names is effective and the services provided are market-oriented so as to promote the development of Internet and e-business in Hong Kong.

4. In October 1999, a Task Force was set up under the Information Infrastructure Advisory Committee (IIAC)¹ to review the administration of Internet domain names in Hong Kong, with a view to recommending a framework of arrangements which best suited our needs. Based on the recommendations made by the Task Force in May 2000, we conducted a public consultation exercise from June to July 2000. The results revealed that there was general support for the proposal that the Joint Universities Computer Centre (JUCC), the current administrator of ".hk" domain names, should gradually transfer the Internet domain names administration functions to a new non-profit-making and non-statutory corporation. This new corporation would assume the overall responsibility for Internet domain name administration in Hong Kong. There was also public support for the adoption of a more flexible domain name registration policy, including accepting registration of multiple domain names for a company, allowing transfer of domain names, and creating a new second level domain category under ".hk" to enable registration by individuals. The public also supported the establishment of an alternative dispute resolution mechanism to facilitate early resolution of domain name disputes so as to obviate the need to resort to court settlement.

5. Following the announcement of the public consultation results, JUCC established a provisional board, with representatives from the universities, industry and the Government in December 2000, to take forward the proposals supported during the consultation exercise. As it would take time to set up a new corporation to take over the domain name administration functions, JUCC set up a company, the Hong Kong Domain Name Registration Company Limited (HKDNRCL), to implement the new domain name registration and dispute resolution policies starting from 1 June 2001, so as to benefit the Internet community early.

/Establishment

¹ The IIAC was established in August 1998 to advise the Government on the ways and means to promote the development of Hong Kong into a leading digital city. It is chaired by the Secretary for Information Technology and Broadcasting, with members drawn from a wide cross-section of the industry, business community and the academic field.

Establishment of the HKIRCL

6. In June 2001, a Preparatory Committee was set up to develop the constitution of a new corporation to administer domain name registration, and to work on the preparatory arrangements for the transfer of the domain name administration functions from JUCC to the new corporation. The Preparatory Committee comprised representatives from JUCC; the IT, commercial and legal sectors; the Consumer Council and the Government. The Preparatory Committee decided that the new corporation should be named as "Hong Kong Internet Registration Corporation Limited". HKIRCL was incorporated in December 2001 and its Board of First Directors, basically mirroring the membership of the Preparatory Committee, was formed in January 2002.

7. Within twelve months of its incorporation, HKIRCL will implement a membership scheme with its members to be recruited from ".hk" domain name holders, Internet service providers, the IT industry, the commercial sector and academia. Its Board of Directors will be elected from its members, with the Government represented on a permanent basis to provide input pertaining to public policies. The Board will consist of 13 directors as set out in Enclosure 1.

Encl. 1

8. The transfer of the domain name administration functions will be effected through transfer of shares of HKDNRCL from JUCC to HKIRCL. Before HKIRCL can take over the domain name administration functions, it will have to secure a start-up working capital to fund its initial operations and capital investment for rolling out new registration services.

9. In its first year of operation, HKIRCL will need to make a capital investment of about \$3 million for rolling out new services, including registration of domain names for information providers ending with ".info.hk", individual domain names ending with ".name.hk", permanent e-mail accounts ending with ".name.hk" for individuals, and half Chinese domain names ending with ".hk" (e.g. 甲乙.公司.hk). The roll-out of new domain name registration services will help promote e-business in Hong Kong and the development of Hong Kong into an Internet hub.

10. Moreover, in recognition of JUCC's pioneering work and contributions in setting up the ".hk" domain name administration regime, HKIRCL has agreed to pay a sum of \$10 million to JUCC. To ensure that the payment will not impose undue financial burden on HKIRCL, JUCC has agreed that the payment would be made from the net profit of HKIRCL and that no payment is required for a year if HKIRCL does not make any profit in that year. It is anticipated that the \$10 million payment can be fully discharged in six years.

11. To ensure that HKIRCL will have sufficient funds to start and maintain its operations in the initial years, commercial banks have been approached for loans but without success as HKIRCL is a new company without a proven track record or any collateral.

Financial support to the HKIRCL

Encl. 2

12. As can be seen from the illustrative cash flow projection at Enclosure 2, HKIRCL will need a loan of \$6.5 million to start and maintain its operations in the initial years. The proposed terms and conditions of the loan are as follows -

- (a) Repayment terms: HKIRCL will repay the loan by seven equal annual installments (covering loan principal and interest) beginning on the third anniversary of the date of the first draw down. Interest accrued in the first two years will be capitalized. HKIRCL may repay the loan in whole or in part at any time ahead of the repayment schedule. In case HKIRCL has unexpected cash flow problems to repay the loan, it may amend the repayment schedule or extend the loan repayment period with the prior approval of the Financial Secretary; and
- (b) Interest rate: HKIRCL will pay interest on the loan at a rate equivalent to the average of the best lending rates quoted by the note-issuing banks in Hong Kong.

13. Detailed terms of the proposed loan will be set out in a loan agreement to be entered into between the Government and HKIRCL.

FINANCIAL IMPLICATIONS

14. The loan amount proposed is \$6.5 million and the bulk of it is expected to be drawn down in 2002-03. The loan is expected to be repaid from 2004-05 to 2010-11. Based on the assumption that the proposed loan will be drawn in one-go in 2002-03 and the best lending rate throughout the loan period will be 7.5% p.a., the total interest payable (including capitalized interest) is estimated at \$3.4 million.

CONTROL MECHANISM

15. HKIRCL is a non-statutory, non-profit-making company limited by guarantee, with no share capital. The operation and financial position of HKIRCL will be closely monitored by its Board of Directors. The Government has a permanent seat (represented by the Information Technology Services Department) on HKIRCL's Board.

16. Separately, the Government will endorse the application of HKIRCL to the Internet Corporation for Assigned Names and Numbers (ICANN) seeking the latter's delegation to HKIRCL to administer ".hk" domain name registration in Hong Kong. HKIRCL will be designated as the ".hk" domain name administrator with the mandate to exercise the registration functions in Hong Kong and represent Hong Kong in international Internet forums. The tripartite relationship amongst ICANN, the Government and HKIRCL will be set out in a memorandum of understanding (MOU) to be signed between the Government and HKIRCL. Under the MOU, HKIRCL will undertake to work cooperatively with the Government within the public policy objectives of the latter.

BACKGROUND INFORMATION

17. HKIRCL will be the administrator of the country-code top-level domain (".hk") of Hong Kong. A domain name locates an organisation or other entity on the Internet. The domain name space is constructed as a hierarchy. It is divided into top-level domains (TLD) which are further divided into second-level domains and so on. There are two types of TLDs: country-code (ccTLD) and generic (gTLD). ccTLDs (e.g. ".hk", ".cn", ".au", etc.) define the name of a country/economy and are administered by their corresponding governments or organisations with the government's acquiescence. gTLDs (e.g. ".com", ".org", ".net", etc.) are created for use by the Internet community and they represent the business nature of the segment of the domain name space. The ".hk" ccTLD is a public resource of the Hong Kong Special Administrative Region. JUCC, the current administrator of the ".hk" ccTLD, will transfer the administration functions to HKIRCL. After the transfer, HKIRCL will be responsible for administering the ".hk" ccTLD to meet the needs of the local Internet community.

18. One of the initiatives in the 2000 Policy Objective for the Information Technology and Broadcasting Bureau is “to keep the administration of Internet domain names in line with international development trends so as to promote the extensive use of the Internet”. The new arrangements under this initiative, which were formulated based on the results of a public consultation exercise conducted in mid-2000, include the implementation of new Internet domain name registration policies and the establishment of a new non-profit-making and non-statutory corporation for assuming the overall administration of Internet domain names in Hong Kong.

19. On 8 February 2002, we consulted the Legislative Council Panel on Information Technology and Broadcasting on the proposed loan to HKIRCL. The Panel supported the proposal.

Information Technology and Broadcasting Bureau
March 2002

**Membership of the Future Board of Directors
of the Hong Kong Internet Registration Corporation Limited**

Class	Members in the Class	No. of directors to be elected by members
User	".hk" domain name holders	6
Service Provider	Internet service providers and (future) domain name registrars	2
IT Industry	IT industry organisations whose members are eligible to vote in the Legislative Council election in respect of the IT Functional Constituency as defined in the Legislative Council Ordinance	2
Commerce & Industry	Commerce & industry organisations whose members are eligible to vote in the Legislative Council election in respect of the Commercial and Industrial Functional Constituencies as defined in the Legislative Council Ordinance	1
Tertiary Institution	Joint Universities Computer Centre	1
Government	Government (represented by Information Technology Services Department)	1 (permanent representative)

Enclosure 2 to FCR(2001-02)69

Hong Kong Internet Registration Corporation Limited

Cash flow Projection for 2002-03 to 2010-11

	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>
\$'M									
Cash generated from operation	(2.200)	0.210	2.880	4.820	7.490	9.420	12.100	14.020	16.710
<i>Less</i>									
Interest payment to HKSARG	-	-	(0.563)	(0.499)	(0.430)	(0.356)	(0.277)	(0.191)	(0.099)
Taxation payment	-	-	-	(0.530)	(1.102)	(1.507)	(1.936)	(2.243)	(2.674)
Net cash generated	<u>(2.200)</u>	<u>0.210</u>	<u>2.317</u>	<u>3.791</u>	<u>5.958</u>	<u>7.557</u>	<u>9.887</u>	<u>11.586</u>	<u>13.937</u>
<i>Less</i>									
Capital Expenditure	(3.000)	-	-	-	-	-	-	-	-
Payment to JUCC	-	(0.105)	(1.440)	(2.410)	(3.745)	(2.300)	-	-	-
Interest Payment to JUCC	-	-	-	-	-	(0.115)	-	-	-
	<u>(5.200)</u>	<u>0.105</u>	<u>0.877</u>	<u>1.381</u>	<u>2.213</u>	<u>5.142</u>	<u>9.887</u>	<u>11.586</u>	<u>13.937</u>
<i>Add</i>									
Draw down of proposed loan	6.500	-	-	-	-	-	-	-	-
<i>Less</i>									
Repayment of proposed loan	-	-	(0.855)	(0.919)	(0.988)	(1.062)	(1.142)	(1.227)	(1.319)
Net cash flow for the year	<u>1.300</u>	<u>0.105</u>	<u>0.022</u>	<u>0.462</u>	<u>1.225</u>	<u>4.080</u>	<u>8.745</u>	<u>10.359</u>	<u>12.618</u>
Balance brought forward	-	1.300	1.405	1.427	1.889	3.114	7.194	15.939	26.298
Balance carried forward	<u>1.300</u>	<u>1.405</u>	<u>1.427</u>	<u>1.889</u>	<u>3.114</u>	<u>7.194</u>	<u>15.939</u>	<u>26.298</u>	<u>38.916</u>

Interest rate: Assuming that the best lending rate is 7.5% p.a.