

MEMORANDUM

TO: Legal Sub-team of the Cross-Community Working Group
on Enhancing ICANN Accountability

FROM: Sidley Austin LLP and Adler & Colvin

RE: Use of Unincorporated Associations in ICANN Governance

DATE: May 3, 2015

Overview

This memorandum revises and supplements our responses of April 23, 2015, and May 1, 2015, to questions regarding unincorporated associations. It includes a brief description of the proposed uses of unincorporated associations, addresses questions raised to date, and attaches a draft example of Articles of Association that would evidence formation of an unincorporated association as a legal entity for an SO or AC to exercise voting rights as a member or designator of ICANN.

Proposal

Whether the SO/AC membership model or SO/AC designator model is implemented to increase ICANN accountability, we recommend that any SO or AC that will name directors to the ICANN board be established as a legal person to comply with corporate law requirements (in the case of SO/AC membership) and to allow member and designator rights under bylaws or contractual arrangements to be enforced. One form of legal person under discussion is the unincorporated association, available throughout the U.S., but in a particularly robust form for nonprofits under California's law.

As proposed, the SOs and ACs would continue to exist and function as they have in the past, but each SO and AC that will exercise rights as a member or designator will establish an unincorporated association as a separate legal entity controlled by the SO or AC. Such a recognized legal entity is necessary to:

- hold the membership or designator status and the rights of a member or designator under ICANN's governing documents;
- enter into any contract that may be needed to implement accountability mechanisms; and
- enforce rights under governing documents and contracts as needed.

Each SO and AC with an unincorporated association could continue to follow its current processes for decision making including in causing the legal entity to act, or it could provide for other processes for determining who within the SO or AC would be authorized to cause the unincorporated association to take any action or exercise any right and under what circumstances. These decision processes would be incorporated into the ICANN Bylaws and/or the unincorporated association's Articles of Association. (This is a legal detail to be worked out, but most likely there would be cross reference between these documents.) Alternatively, the ICANN Bylaws could set out rules applicable to all SOs and ACs regulating their internal decision-making.

It would also be possible to organize the unincorporated associations as the SOs or ACs themselves, not as separate legal shells, so that all the activities of the SO or AC currently conducted in relation to ICANN would instead be conducted within the new unincorporated associations. However, such an approach may involve greater disruption to current arrangements, complexity in ICANN's governance, administrative effort, and operational burdens placed on the unincorporated associations that, today, are undertaken within ICANN.

Q&A

Please find below questions and answers, provided on a general level in keeping with the level of the questions. Please note that we make the same qualifications as in prior memoranda distributed to the Legal Sub-team.

Question: **What are the administrative formalities to create an unincorporated SO/AC?**

Response: Under California law, the requirements for forming and operating an unincorporated nonprofit association are minimal and there is great flexibility. Basically the group needs to set out their basic rules and define who members shall be. Simple steps would include:

- Prepare articles of association or another document in the nature of a charter, as the governing document for the group that:
 - describes who qualifies to participate
 - establishes a governance mechanism for decision-making by the participants
 - sets basic procedures for meetings of the participants and
 - addresses any other key management functions that are necessary for the association to operate

Currently the ICANN bylaws address substantially all of these requisites. We have therefore suggested that the unincorporated association governance documents simply cross-reference provisions of the ICANN bylaws to avoid duplication and potential inconsistency. A sample of minimal articles of association is attached as Annex A.

- File a statement with the California Secretary of State (there is a prescribed online form) indicating the association's principal address and its agent for service of process in California. This could be the same as ICANN's. This will establish a record with regulatory authorities of the unincorporated association's existence, and will help ensure that it can avail itself of California's protective provisions benefitting such associations.

Question: Who (legal persons or individuals) would have to fulfill these formalities? Each member? the Council? The Chair?

Response: These minimal formalities would need to be fulfilled by the group and could be delegated to as few as two persons on behalf of the group, for approval by the initial participants. Each unincorporated association would establish and articulate a governance structure in a governing document such as articles of association or a charter, as described above. Officers are not required but could be selected, or the group could designate one or more of its participants to undertake the effort to make sure that the minimal formalities are observed.

Question: Are there any "Officers" or equivalent for such unincorporated SO/AC?

Response: An unincorporated association is not required to have officers. It may have officers if it so desires, but this is not a legal requirement.

Question: Is there any requisite in terms of funding?

Response: The law does not prescribe any requirements for funding. As with whether or not to have officers, there is flexibility. For example, as in the sample in Annex A, the unincorporated association's purpose and activity could be limited to participating as a designator or member of ICANN, and if so, it may not need any funding at all, nor would it need to hold any assets.

Question: Does participation of an organization (such as a ccTLD manager) into such an unincorporated SO/AC extend the possibilities that it be sued in the US?

Response: If an organization which is a current participant in ICANN's governance through an SO/AC also participates in that SO/AC's unincorporated association, it will not expose the organization to any greater liability than it already has as a participant in ICANN, as discussed further below in the last question. ICANN is a nonprofit public benefit corporation and, under California law, as well as the ICANN bylaws, participants in the governance of ICANN generally would be indemnified by ICANN from liability. The California Corporations Code expressly provides that members of a nonprofit unincorporated association are not liable for the obligations of the association. In addition, it would also be possible for ICANN to continue to provide indemnification for participants in the unincorporated associations that are ICANN's volunteers or otherwise participate in ICANN's governance.

Question: Can an unincorporated SO/AC be sued? In that case, who would have to pay the legal fees?

Response: Yes, an SO/AC's unincorporated association could be sued, as it would be considered a separate legal person under the law. It would also have the capacity to sue others (important for enforcing rights). With regard to legal fees, the default rule in the United States is that each party to a lawsuit bears its own fees and costs, and rules vary by jurisdiction elsewhere. However, the legal fee burden may be shifted by contract. For example, ICANN could have a contract with an SO/AC's unincorporated association entity that provides that ICANN will pay the legal fees of a member (or designator) who brings suit against ICANN, and conversely, to cover the legal fees of an association (member or designator) that is sued for its work supporting ICANN.

Question: Is there any fiduciary responsibility of liability attached to being a member of an unincorporated association to being a council member? to being chair?

Response: Members of unincorporated associations do not possess fiduciary duties via the California Corporations Code. Nor do officers of unincorporated associations. Instead, the duties and obligations of members and officers are as set forth in the association's governing documents. The governing documents are contractual in nature and can be drafted with great flexibility.

With regard to liability, members, officers and agents are not individually or personally liable for the association's debts or liabilities on the sole basis of their relationship with the association.

Question: Would creating an unincorporated association prevent an SO/AC (ex: ccNSO) from further structural reviews of the SO/AC as foreseen by the ICANN Bylaws ?

Response: The creation of an unincorporated association shell for an SO/AC under California law should not require any change in the procedures set forth in the existing bylaws of ICANN with respect to the SO/AC, although some bylaws provisions may be desirable to standardize how each SO or AC uses its unincorporated association. Indeed, as exemplified in the sample in Annex A, we had contemplated that the organizational documents of the unincorporated associations would be very short, indicating that the procedures for the governance of each such association are those set forth in the ICANN bylaws, as supplemented by any existing rules or procedures adopted by each SO/AC. Once unincorporated associations have been established, the functions and processes of each SO or AC can continue to evolve under the control of its participants subject to any applicable ICANN Bylaws, through amendments to applicable Bylaws and/or its Articles of Association. If at some future date, the unincorporated associations are no longer needed, they can be terminated with as little formality as they were formed.

Question: What will the control mechanisms be between an SO/AC and its alter ego unincorporated association and how will they be enforced?

Response: The control mechanism for an SO/AC over its unincorporated association could be essentially the same as whatever control mechanisms currently exist to ensure that the SO/ACs do what their participants collectively decide they should do. It is contemplated that

the ICANN Bylaws and/or each unincorporated association's Articles of Association will provide processes for decision making as discussed above. These governing documents could provide that membership in the unincorporated association is identical to the participants in the related SO/AC. Alternatively, the governing documents could provide that the unincorporated association's membership is determined by the related SO/AC.

- In the first instance, perfect identity between unincorporated association membership and SO/AC participants avoids any control issues: the unincorporated association will only behave as the participants in the SO/AC determine since they are the membership of the unincorporated association.
- In the alternative instance, where the SO/AC determines membership in the unincorporated association but there is not complete identity between the two groups, control will lie in the ability of the SO/AC to select the membership of the unincorporated association. In the unlikely event that a dispute arises over how the unincorporated association acts, the SO/AC can replace members in the unincorporated association. If a dispute arises as to membership of the unincorporated association, the SO/AC will designate the group constituting the appropriate membership and that group will be able to seek enforcement in court if necessary to assert its rights over any "rogue" or "invalid" group claiming to control the unincorporated association.

Question: As an example, what mechanism would the ccNSO use if ccUA (the alter ego unincorporated association created as the legal entity for ccNSO) was not acting on the instructions of the ccNSO? Assume that ccUA had 5 members selected by ccNSO but in a dispute the 5 members refused to act in ccNSO's interests and also refused to step down.

Response: Please see the answer immediately above. Assuming that ccUA was established with 5 members and the governing documents (ICANN Bylaws and/or ccUA Articles of Association) provide that the ccNSO selects the 5 members and can remove those members at will and replace them, the ccNSO would replace those members if ccUA did not act in the interests of the ccNSO. Should the ccNSO decide to replace the members of ccUA and select 5 new members but the old members "refused to stand down," the new group of 5 members would be able to go into court as the validly formed ccUA in an action to enforce their rights in the dispute with the "rogue" or "invalid" ccUA.

Question: How would being formed into unincorporated associations affect the potential liability exposure of (possible future) members of ICANN in foreign jurisdictions? In particular, whether status as an unincorporated association in California would be recognized by a foreign jurisdiction?

Response: Under general principles of international law, the basic conclusions are:

- being formed into an unincorporated association under California law would only lessen the potential liability of participants in that association
- California law likely determines the legal status of the unincorporated associations in foreign jurisdictions

This issue presents a “choice of law” question, that is, which law applies, the law of California or the law of the foreign jurisdiction. The answer is that the law of the state of organization (California law in this case) should be selected to determine the member’s legal status, at least with respect to its relationships with ICANN. The selection of California law stems from either a choice of law provision in ICANN’s bylaws or other agreements with its members (for simplicity, we assume here that ICANN will have members) or through general principles of choice of law that govern the internal affairs of entities.

- In the case of a dispute between ICANN and its members (or between two members), the dispute resolution procedures in the bylaws (or related contracts) would specify IRP and arbitration, with a waiver of standing challenges. In this instance, the status of the member would not be an issue. However, if the disputing party were able to escape arbitration, the choice of law provision in the contract or other document that governs the relationship between the parties would determine the governing law. Contracting parties generally can anticipate and resolve jurisdictional issues by agreement. Even if ICANN sued one of its members in a foreign jurisdiction or two members were to sue each other, the agreed choice of law provision should govern and determine status as an unincorporated association and resulting limitations on liability. Although we did not survey this issue globally, these choice of law rules are generally accepted (excluding areas without a reliable rule of law).
- If the unincorporated association were sued by a third party or by a member outside the bounds of the contract, California law governing status as an unincorporated association would still likely apply. In the United States, the “internal affairs doctrine” recognizes that the state in which an entity is organized has an interest regarding its status. Analogous principles generally apply elsewhere globally to recognize the jurisdiction where an entity is organized or has its seat of authority. Internal affairs generally include the organizational structure and the relationships between the participants in the organization. This doctrine also has been interpreted to include an entity’s capacity to sue or be sued because such capacity is deemed an internal affair established by state law. We should note, however, that some jurisdictions approach these issues with multi-factored tests that consider the interests of the respective countries, but we have endeavored to provide a clear statement of the most common approach.

In sum, the status of an unincorporated association organized under California law should generally be recognized in a foreign jurisdiction under a contractual choice of law provision and/or the internal affairs doctrine.

Regardless of whether the entity is formed into an unincorporated association, the individual participants in the ICANN member should not face any greater liabilities than they face now based on their activities with respect to ICANN. Even if some foreign jurisdiction were to disregard the existence of a California unincorporated association, participants in that group would not be subject to any greater liability than they are now. At present, the individuals bear personal liability for their actions. If the association were to be disregarded, they would still have the same personal liability for their actions. Thus, organizing the participants into an unincorporated association under California law would not make the participants worse off.

ANNEX A

DRAFT EXAMPLE ARTICLES OF ASSOCIATION

[Attached]

DRAFT EXAMPLE

This draft example is provided to help explain legal counsels' recommendation that SOs and ACs need to exist as unincorporated associations in order to be able to be members of ICANN and enter into contracts, and enforce their rights as members and under contracts. This example contains the bare minimum of provisions we recommend, and should not be considered a final template for creating such entities, as many details have yet to be worked out, and significant changes are to be expected.

ARTICLES OF ASSOCIATION of [NAME of SO/AC] MEMBER ENTITY

PURPOSES

Section 1. General Purposes. This association is organized as a nonprofit association under Section 18000, et seq. of the California Corporations Code (the "Code") for common lawful purposes and is not organized primarily to operate a business for profit.

Section 2. Specific Purposes. This association is formed specifically and solely to exercise, enforce, and defend its membership, contract, and other rights established by or under the Bylaws of the Internet Corporation for Assigned Names and Numbers, a California nonprofit public benefit corporation ("ICANN"), with regard to the governance of ICANN.

RELATIONSHIP TO [NAME of SO/AC]

This association is established on behalf of all those who participate in [NAME of SO/AC] under the portions of the ICANN Bylaws and other rules pertaining to the [NAME of SO/AC]. The separate existence of this association outside of ICANN shall not affect the continued functioning or operations of [NAME of SO/AC] within ICANN. This association shall not receive, hold, or manage any money or other tangible property

GOVERNANCE AND POWERS

The governing structures and principles of this association, and all other matters affecting its organization and operation, including but not limited to determining who has the authority to officially act on behalf of this association and how such authority shall be evidenced, and the process for amending these Articles, shall be prescribed under the ICANN Bylaws or other rules established by [NAME of SO/AC] pursuant to the ICANN Bylaws. This association shall have powers and authority to the fullest extent permitted by law to an unincorporated nonprofit association.

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