

2017

Financial statement

Finance

On 1 January 2017, through our subsidiary SIDN Deelnemingen B.V., we acquired a 65 per cent majority interest in Connectis Group B.V. of Rotterdam. The acquisition price was € 8,612,500. We additionally agreed an earn-out arrangement in the form of a loan of € 812,500. The loan will be repaid out of future dividend payments. In the annual financial statement for 2017, the majority interest is accounted for as a participating interest; hence Connectis Group B.V.'s result for 2017 is included under 'Result from participating interests'.

Our financial position remained strong in 2017. The net result for the year was a loss of € 645,200. The result will be charged to the general reserves. At the close of 2017, our equity capital was € 32,131,800. The equity capital serves partly as a financial buffer, helping to assure the organisation's continuity. The minimum financial buffer required is related to the organisation's structural cost base. The cost base rises over time, as the organisation grows and the quality, stability and security requirements increase. It is therefore necessary to enlarge the financial buffer as well. The financial buffer is currently ample to provide necessary and reasonable cover against the identified risks and uncertainties.

The operating result for the year was a loss of € 19,300. That represents a reduction of € 3,360,100 relative to 2016 (€ 3,340,800). The reduction is attributable to a donation of € 1,651,500 to SIDN Fund in 2017, depreciation of € 904,200 in the value of the goodwill acquired with the majority interest in Connectis Group B.V., and a € 1,098,000 increase in personnel costs. Corrected for the donation to SIDN Fund, the operating result for 2017 is € 1,632,200. As a percentage of turnover, the operating result was -0.1 per cent (2016: 17.0 per cent). Our share in Connectis Group B.V.'s net result for 2017 was a loss of € 169,100.

Net turnover was € 19,705,000: € 90,000 higher than in 2016 (€ 19,615,000). That corresponds to a year-on-year rise of 0.5 per cent, whereas 2016's net turnover had been 1.8 per cent higher than the previous year. The increase in turnover was mainly the result of higher income from both domain name registrations and new activities. The .nl domain contained more than 5.794 million domain names at the end of the year. In 2017, the net growth in the number of registered domain names was 109,706: slightly more than the growth of 80,529 domain names in 2016.

In order to promote the use of DNSSEC to secure domain names, we have been paying an annual rebate per secure domain name since July 2012. By the close of 2017, approximately 2.855 million domain names were secured with DNSSEC (49.3 per cent of all .nl domain names). In 2015, we started the Registrar Scorecard: an incentive programme designed to further increase the quality of the .nl zone. Through the programme, we returned € 517,000 to participating registrars in 2017 (2016: € 280,000). The total value of all the incentives set off against the turnover (DNSSEC discount, Registrar Scorecard rewards, volume

discount and direct debit discount) was € 3,213,000: a 15 per cent increase on the 2016 total of € 2,800,000.

The number of registrars fell again, to stand at 1,303 at the close of 2017 (2016: 1,372). That had a negative impact on net turnover of € 48,000. Turnover from new activities was € 687,000 in 2017, an increase of 35 per cent on 2016 (€ 509,000).

In 2017, several SIDN employees were attached to Connectis. The associated costs of € 160,000 were charged to Connectis; that sum was partially offset by the hire of temporary personnel.

Our expenditure rose in 2017 by € 3,450,000 (21.1 per cent). Total expenditure in 2017 was € 19,724,000, compared with € 16,274,000 in 2016. The rise is attributable to a donation of € 1,651,500 to SIDN Fund, depreciation of € 904,200 in the value of the goodwill acquired with the majority interest in Connectis Group B.V., and increased personnel costs of € 1,098,000.

Personnel costs were € 1,098,000 higher than in 2016, at € 8,794,000 (2016: € 7,696,000).

The rise is attributable partly to growth of the workforce and general pay rises (together € 302,000) and partly to higher social security contributions (€ 136,000). The increase in the size of the workforce was due to the expansion of SIDN Labs' research capacity and the establishment of a Security Operations Centre. Expenditure on temporary personnel increased by € 649,000, as a result of delays filling certain vacancies and the need to provide cover for personnel on sick leave. The average size of the workforce rose from eighty-four FTEs in 2016 to eighty-six FTEs in 2017; the total number of people employed at the end of 2017 was ninety-eight, up from ninety-one at the end of 2016.

Depreciation costs in 2017 were € 1,858,000. That is € 453,000 higher than in 2016 (€ 1,405,000). Depreciation of € 904,200 in the value of the goodwill acquired with the majority interest in Connectis Group B.V. is partially offset by the fact that certain fixtures and fittings have now been fully written off; hence depreciation of € 347,000 in 2016 did not recur in 2017.

The other operating expenses in 2017 were € 8,929,000 (2016: € 7,173,000). The increase of € 1,756,000 relative to 2016 was due mainly to the donation of € 1,651,500 made to SIDN Fund in 2017.

In 2017, total capital expenditure was € 809,000, of which € 642,000 was invested in production systems, € 31,000 in security tooling, € 11,000 in R&D tooling, € 91,000 in office ICT equipment and € 34,000 in fixtures and fittings.

Whereas in 2016 we had a positive cash flow of € 4,094,200, in 2017 we generated a negative cash flow of € 10,338,900, mainly as a consequence of acquiring a majority interest in Connectis Group B.V. (€ 8,612,500). In the course of 2017, we made further loans to Connectis totalling € 1,487,000. In order to manage our liquidity risk, we spent € 1,490,000 on the acquisition of Dutch and German government bonds.

Our solvency fell slightly from 79.8 per cent in 2016 to 76.8 per cent in 2017. In 2017, € 4,908,000 was invoiced and received for services to be delivered in the following calendar year (2016: € 4,323,000).

In 2013, we began talks with the tax authorities regarding the tax implications of the donation to SIDN Fund. SIDN and the tax authorities differ in their view of the extent to which the donation is tax-deductible. Hence, the corporation tax assessment received in respect of 2014 was not in line with the amount that SIDN reported as due on its tax return for that year. We therefore filed an appeal. Hence, the total receivable from the tax authorities is estimated at € 901,500.

Outlook

We anticipate a slight increase in the number of registered .nl domain names in 2018 and a modest corresponding growth in earnings from .nl registrations. Total earnings are likely to increase a little as well. Our workforce is expected to grow, thus pushing up overall expenditure. Capital expenditure is likely to be broadly similar to 2017 and we anticipate that the result from participating interests will be nil in 2018. Taking all factors into account, we envisage a positive operating result and expect to generate a positive cash flow. Our intention is to make a donation of € 2,500,000 to SIDN Fund in 2018.

Risks and uncertainties

Vision and policy

Our strategic plan for the next four years is reviewed and updated annually. As part of that process, we consider the company's (strategic) risk exposure. The management team and staff carry out a context analysis, in which opportunities and threats are surveyed. We also identify the strengths and weaknesses of the internal organisation. The conclusions of the analysis are then translated into a statement of risks and (where appropriate) countermeasures. The primary objectives of risk management are to assure the continuity of the organisation and our role as registry for the .nl domain, and to protect our position and reputation.

Since 2011, we have been ISO27001-certified. That status involves operating an Information Security Management System (ISMS), featuring an annual cycle of business impact analysis, risk identification, risk management and residual risk appraisal, all in accordance with a defined information security policy. The findings of internal and external audits are regularly discussed, e.g. in our Tactical Security Meetings (TSMs), after which any necessary improvements are implemented. The outcomes are monitored by means of biannual management reviews. In that context, consideration is given to the results of the audits and performance assessments, as well as to the status of audit action points and any security incidents that may have occurred.

Before starting a project, we produce a project plan, which always includes a section covering the risks associated with the project, the risk management measures to be taken and residual risks. Before the project is given the go-ahead, consideration is given to the risk section of the project plan. Any changes to the risk situation and the risk management measures are addressed in the regular project progress reports.

Our Supervisory Board oversees our organisation's strategy, policy and general operational position. The Supervisory Board pays particular attention to risk management, which is scrutinised by the Board's Audit Committee and Security & Stability Committee.

Risk analysis and reporting

Strategic risks

The main risks associated with SIDN's strategy stem from the strong dependence on (earnings from) the .nl domain and from the contraction of the .nl market. We do not have a direct sales channel to the end market and therefore have very little scope for influencing that market ourselves. The focus is consequently on collaboration with our registrars, e.g. through the Registrar Scorecard, which offers incentives to promote the use of .nl domain names. At the same time, we are seeking to increase our added value, extend the range of services we offer and reduce our dependence on .nl. It was with those aims in mind that we acquired a 65 per cent holding in Connectis Group B.V. at the start of 2017.

In order to maintain risk separation between SIDN and Connectis Group B.V., we established a subsidiary, SIDN Deelnemingen B.V. at the end of 2016. It is the new subsidiary that holds 65 per cent of the shares in Connectis Group B.V.

Connectis Group B.V. is currently transitioning from start-up to scale-up. It is a young, dynamic enterprise with a strong position and abundant opportunities in a growing and competitive market. In 2017, we invested to facilitate the process of transition, with the emphasis on further professionalisation, realignment of the company's commercial strategy and the creation of synergy and added value.

Our strategic risk appetite is moderate in relation to activities with the potential to increase our added value.

Operating risks

The two main risks associated with our operating activities are interruptions to the availability of our services and breaches of the confidentiality or integrity of important data. Such problems could arise from technical and/or human error, or from deliberate (targeted or indiscriminate) human action. A prolonged, large-scale problem in one of those fields has the potential to threaten the continuity of the organisation in two ways. First, by seriously damaging our reputation, giving rise to doubts in political circles and the community at large as to SIDN's legitimacy as the registry for the .nl domain. Second, by leaving us vulnerable to large compensation claims from clients.

The significance of each key process for service continuity is assessed by means of Business Impact Analysis, which is part of the ISMS. Our DNS services – the basis of the functionality of registered domain names – are the most critical, closely followed by our registration services, which enable users to

register new domain names and to update and cancel existing registrations. Also rated as critical are the Whois/Is, the power supply, our office IT systems, our website www.sidn.nl, and our communication and telecommunication systems.

With a view to assuring availability, integrity and confidentiality, we have put a wide variety of risk management measures in place, designed to minimise the likelihood of problems, and to enable swift corrective action and minimise impact if problems do arise.

The measures in question range from the elimination of single points of failure by extensive redundancy in hardware, software, connections, third-party services and expertise, logical and physical access control, audits and penetration testing, contractual arrangements with suppliers, codes of conduct for SIDN personnel, an emergency backup location, crisis and relocation drills, a privacy board and a Security Operations Centre (SOC).

Our operating risk appetite is low in relation to interruptions to the availability of our services and breaches of the confidentiality or integrity of important data. Our risk appetite in relation to activities with the potential to increase operational excellence is moderate.

Financial risks

- Damage claims and penalties: service interruptions and data confidentiality or integrity breaches have the potential to generate claims and/or penalties. Our General Terms and Conditions limit or exclude our liability for such problems.
- Currency/exchange rate risk: our exposure to currency and exchange rate risks is modest. Our .nl services are priced in euros and we make little use of suppliers that charge us in other currencies.
- Bad debt risk: about 75 per cent of registrars pay by direct debit. Our General Terms and Conditions make provision for action to be taken if a registrar does not fulfil its financial obligations.
- Liquidity risk: our liquid assets are divided across three Dutch banks. In 2017, we acquired a portfolio of Dutch and German government bonds.
- Market risk: our portfolio of Dutch and German government bonds was acquired with a view to holding the bonds until maturity. If circumstance should require us to dispose of the bonds prior to maturity, we would face the risk of the bonds having diminished in value relative to the date of purchase.
- Solvency risk: we maintain a financial buffer to assure the continuity of the organisation (for a period) in the event of a significant loss of our earnings and/or the need for high expenditure at short notice. The minimum size of the buffer increases in step with our structural cost base. The financial buffer is currently well above the defined minimum.
- Uncertainty about our ability to attract finance: to date, we have not needed to seek external finance.

Our financial risk appetite is low.

Legislative and regulatory risks

Changes to national or international legislation and regulations have the potential to affect our organisation and operating processes. We take stock of potentially significant proposed or impending legislative and regulatory changes – e.g. changes in employment law, tax law or data protection law – at an early stage. The impact of any such change is assessed and translated into organisational adaptations, which are then implemented. In view of the potential impact of legislative or regulatory changes relating to our registry role, we have a Legal & Policy Manager with responsibility for that domain. Where necessary and possible, the Legal & Policy Manager seeks to influence the nature of any proposed changes.

We have initiated a comprehensive inventory of our personal data processing activities in relation to the General Data Protection Regulation, which comes into effect in 2018. Each processing activity is being critically examined to determine whether it is consistent with the new legislation. Where necessary, we will modify our procedures to ensure compliance with the law. We have voluntarily appointed a Data Protection Officer.

Our legislative and regulatory risk appetite is low; we endeavour to operate well within the parameters of all applicable legislation and regulations.

Consolidated financial statements for 2017

Consolidated balance sheet as at 31 December 2017 (before appropriation of profit)

Fixed assets

Intangible fixed assets

8,393,948

459,661

Tangible fixed assets

Land and buildings

5,326,488

5,505,908

Machinery and equipment

1,107,138

950,455

Other fixed business assets

789,711

851,561

Tangible fixed assets under development

0

0

7,223,337

7,307,924

Financial fixed assets

4,135,007

987,600

5

Current assets

Receivables

Debtors

303,489

380,696

Tax and social security contributions

363,548

323,440

Other receivables and accrued and deferred assets

1,088,038

954,689

1,755,075

1,658,825

Liquid assets

20,326,724

30,665,580

41,834,091

41,079,590

	31 December 2017 (in €)	31 December 2016 (in €)
Equity capital		
Issued capital	100	0
General reserve	32,776,948	30,232,909
Annual result	(645,208)	2,544,039
	32,131,840	32,776,948
Provisions	0	0
Long-term liabilities	406,250	0
Short-term liabilities		
Liabilities to suppliers	1,113,426	1,100,879
Tax and social security contributions	365,941	336,799
Other liabilities and accrued and deferred liabilities	7,816,634	6,864,964
	9,296,001	8,302,642
	41,834,091	41,079,590

Consolidated profit and loss account for 2017

	2017 (in €)	2016 (in €)
Net turnover	19,704,621	19,614,672
Expenditure		
Wages and salaries	7,243,866	6,195,136
Pension charges	858,797	722,340
Other social costs	691,555	778,569
Depreciation of tangible and intangible fixed assets	2,000,513	1,404,688
Other operating expenses	8,929,196	7,173,153
	<u>19,723,927</u>	<u>16,273,886</u>
7 Operating result	(19,306)	3,340,786
Income from securities	(14,061)	0
Financial income	36,010	45,075
Financial expenditure	0	0
	<u>2,643</u>	<u>3,385,861</u>
Result before taxation	2,643	3,385,861
Taxes	(478,772)	(841,822)
Result from participating interests	(169,079)	0
	<u>(645,208)</u>	<u>2,544,039</u>
Result after taxation	<u>(645,208)</u>	<u>2,544,039</u>

Consolidated cash flow statement for 2017

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	2017 (in €)	2016 (in €)
Cash flow from operating activities		
Operating result	(19,306)	3.340.786
<i>Adjustments for:</i>		
Depreciation and other reductions in value	2,000,513	1, 404,688
	<u>2,000,513</u>	<u>1,404,688</u>
<i>Movement in working capital:</i>		
Receivables	(96,250)	(183,680)
Short-term liabilities	876,965	1,311,703
	<u>780,715</u>	<u>1,128,023</u>
Cash flow from operating activities	2,761,922	5,873,497
Interest received	30,356	129,253
Corporation tax paid	(709,653)	(966,722)
	<u>(679,297)</u>	<u>(837,469)</u>
Cash flow from operating activities (carried forward)	<u>2,082,625</u>	<u>5,036,028</u>

Consolidated cash flow statement for 2017

	2017 (in €)	2016 (in €)
Cash flow from operating activities (carried forward)	2,082,625	5,036,028
Cash flow from investment activities		
Acquisition of participating interest	(243,956)	(100)
Investments in intangible fixed assets	(8,424,855)	0
Investments in tangible fixed assets	(775,767)	(741,738)
Long-term lending	(1,487,260)	(200,000)
Acquisition of securities	(1,489,643)	0
Cash flow from investment activities	(12,421,481)	(941,838)
9 Increase/(decrease) in funds	(10,338,856)	4,094,190
Movement in funds		
Funds as at 1 January	30,665,580	26,571,390
Increase/(decrease) in funds	(10,338,856)	4,094,190
Funds as at 31 December	20,326,724	30,665,580

Colophon

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