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February 21, 2019

To the board members of the Vinton Municipal Electric Utility,

Last week's vote to award a contract to begin construction of a municipally-owned broadband network is troublesome, as this project does not seem financially viable.

A 2017 study assessing the financial performance of more than a dozen municipal fiber networks reported that the median construction cost per household for these networks was \$2,215.<sup>1</sup> At a total price tag of nearly \$8.5 million (or roughly \$3,900 per household/business), Vinton is spending 75% more on a per location basis for its network than the median cost for comparable municipal fiber networks. Even if you had a monopoly on internet, video and phone services, financial viability would be a stretch based solely on the incredibly expensive nature of this project. But therein lies the problem – unlike the monopoly power enjoyed by your municipal electric utility, Vinton is entering a highly competitive market with its communications utility.

The feasibility study prepared by your well-paid consultants is based on the fundamentally flawed assumption that Vinton will achieve a 40% internet take rate in year 1 growing to 62% in year 5. The publicly available data on take rates for other internet providers, whether they be municipally-owned providers or publicly-traded national providers, makes your consultants' projections difficult if not impossible to achieve in a competitive market like Vinton.<sup>2</sup> Keep in mind, these completely unrealistic take rates are what you need just to "break even," meaning that this project doesn't provide positive cash flow until year four and doesn't show any net income until year five. Failure to obtain those overly-aggressive take rates will lead to failure of the entire communications utility.

Furthermore, as I understand the situation, Vinton is planning on financing this project through revenue bonds – the old "if you don't use it, you don't pay for it" scheme. Nothing could be further from the truth. The reality is that by issuing both communications utility revenue bonds and electric utility revenue bonds, and by using your electric utility's surplus funds for this project, Vinton's electric ratepayers (which include each and every household and business in Vinton regardless of whether they sign up for communications services) will be forced to pay higher rates for electricity to pay off the electric utility revenue bonds. Have the citizens of Vinton been told about this possibility/likelihood?

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<sup>1</sup> See Municipal Fiber in the United States: An Empirical Assessment of Financial Performance at <https://www.law.upenn.edu/live/files/6611-report-municipal-fiber-in-the-united-states-an>

<sup>2</sup> Joanne Hovis of CTC Technology and Energy, the consultant representing the municipal fiber network owned by the City of Tacoma, WA, states that based on the experience of other markets, "37 percent is at the high end of what the firm has seen in other markets" and that "it is possible to have a rate of 15 percent or less." Hovis goes on to say that even if internet were priced at a very low \$22 per month, it "would be a great accomplishment" to achieve a 37 percent take rate. See <https://tacomaweekly.com/news/public-option-for-click-network-would-skip-cable-tv/>

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This kind of advice has been given by consultants before, resulting in broadband network failures and millions of taxpayer and ratepayer dollars being wasted. For example, just two months ago, Lake County, Minnesota was forced to auction off its municipal broadband system, only three years after construction was complete. Built at a price of \$90 million, the auction garnered only \$8.4 million – 9 cents on the dollar – leaving the local taxpayers of Lake County on the hook for \$25 million and federal taxpayers on the hook for an additional \$45 million.

These problems are not limited to other states. In Muscatine, Iowa, the city's electric utility loaned more than \$35 million to its communications utility to expand and upgrade its broadband system. A few years later, the electric utility was forced to forgive \$25 million of this inter-department loan and reduce the interest rate on the remaining balance from 3.5% to 0.5%, followed by increased electricity rates in the subsequent years. The electric rate payers paid for the \$25 million that was ultimately forgiven. In other words, each and every household and business subsidized the communications utility project through higher electric rates.

I have no doubt the consultants and advisors you hired said that this project is financially feasible, and that the use of electric utility funds, whether directly or through loans to the communications utility, is acceptable. Even if the electric utility funding mechanism is legal (and I question whether it is under Iowa law), I believe it is imperative that your electric utility consumers be fully informed of the risks you are taking on in connection with this project. That would be the responsible thing to do.

Thank you for your time in considering the points made in this letter. I know your job is not an easy one. Vinton is a wonderful community, in large part because of the efforts by you and others to make it that way. I hope, however, that the risks taken on by this project don't set the community back for years to come.

I would be happy to discuss this further if you would like.

Sincerely,



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