



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Chief of Staff

June 21, 2018

Mr. Jeffrey Dykes, CEO
and Board of Directors
BrightRidge
P.O. Box 1636
Johnson City, TN 37605

Dear Mr. Dykes and Members of the Board:

Our office received a detailed business plan (the "Plan") on April 25, 2018, for the Johnson City Energy Authority dba BrightRidge to provide internet services. BrightRidge submitted the Plan pursuant to T.C.A. §§ 7-36-107(a)(6)(B) and 7-52-602, which states that the Office of the Comptroller "shall provide a written analysis of the feasibility of the proposed business plan."

The Plan was prepared by BrightRidge with the assistance of its Consultant, Magellan Advisors. We have not attempted to compare the information included in the Plan to industry standards, nor are we aware of any such industry standards for governmental entities providing these types of services. Our feasibility analysis is based on a limited review of the Plan submitted, and our expectation that the governing body of BrightRidge reviewed the Plan before submitting it to our office. During our review process, we requested additional information we felt would be helpful in reviewing the Plan. We also requested that certain revisions be made to the Plan to comply with statutes and provide clarity.

Based on our review of the information in the Plan, including revisions and additional documentation submitted by BrightRidge, we could not determine if the proposed Plan is feasible.

The uptake rate, or the percentage of potential electric customers who will also purchase broadband service from BrightRidge, is the key assumption for the projection of future revenues to make the proposed broadband division fully self-supporting. Sufficient revenue to meet all expenses of operation and maintenance, including reserves for operations and capital maintenance and meet all debt service obligations is the primary factor in determining if the Plan appears to be financially feasible. The Plan's market analysis did not appear to support the projected uptake rate. We could not determine if the revenue projections were reasonable due to uncertainties concerning the broadband uptake rate projections.

BrightRidge's consultant projects an uptake rate of 45% and 40% for broadband fiber residential and business customers, respectively, by the year 2022 increasing to 48% and 43%, respectively, by 2035. The uptake rate for both residential and business broadband wireless customers is projected to be 15% in 2022 and is projected to increase to 18% by 2035.

The Plan's uptake rate assumptions are based largely on the ability to attract current subscribers from other providers; however, the Plan does not address the impact of market competition on pricing. The Plan did not provide adequate assumptions, or a methodology, to support the uptake rates given the number of existing service providers in the service area. Because the Plan did not consider the impact of market competition to the population of customers that currently have service, we could not conclude the reasonableness of the uptake rate and therefore could not determine if the Plan as presented is feasible.

Analysis

Our analysis is based upon the following assertions as presented in the Plan, including the additional information requested, submitted to this office:

1. The project is based on BrightRidge's electric division having deployed a Smart Grid network infrastructure. This infrastructure along with an expanded fiber network and wireless antennae will allow BrightRidge to offer high-speed internet service to its electric customers in its service area.
2. During the period 2019 through 2025, interdivisional loans of approximately \$62,300,000 will be made from the electric division to the broadband division to fund construction and equipping of the fiber feeder/distribution system and associated equipment and to provide working capital needs during the start-up phase. The loans will have a 4.0% interest rate with the final maturity payment in 2038.
3. In a letter dated May 30, 2018, BrightRidge responded to several questions and concerns expressed by our office concerning its Plan. A revised presentation of the original Plan narrative and financial analysis was also provided. The revised Plan included an analysis to support BrightRidge's ability to make interdivisional loans from the electric division to the broadband division. The analysis included amounts for pole attachment fees, lease revenue and interest income that will be charged to the broadband division by the electric division as well as principal repayment amounts from the broadband division for the interdivisional loans.
4. BrightRidge intends to provide video service using National Cable Television Cooperative as its provider for video services. Telephone service was not part of the revised Plan.

BrightRidge should consult with its legal counsel to ensure they comply with all aspects of state statutes.

5. The broadband division will offer the following services at the listed average pricing:

Service Rates	
Residential Fiber	Monthly Rate
Double-Play Premium ARPU	\$ 145.00
Double-Play Standard ARPU	130.00
Internet Only ARPU	60.00
Residential Wireless	
Internet Only ARPU	60.00
Business Fiber	
Internet Premium ARPU	300.00
Internet Standard ARPU	200.00
Business Wireless	
Internet Only ARPU	\$ 100.00
* ARPU - Average Revenue Per User	

6. The Plan identifies BrightRidge electric customers as the target market for the new broadband division. We could not determine the reasonableness of the projected uptake rate for residential broadband fiber customers of 45% by 2022. The Plan's uptake rate assumption of 45% of current residential electric customers is based largely upon the ability to attract current subscribers from other providers; however, the Plan does not address the impact of market competition on pricing. The uptake rate is the key assumption for the revenue projections that support the financial feasibility of the proposed broadband division.
7. On the pro forma schedules provided in the Plan, the broadband division estimates losses in the first three fiscal years (2019-2021). The cost of leasing the fiber optic network infrastructure is included as an operating expense. It is projected that in fiscal year 2022, or year four, the broadband division will generate income in the amount of \$185,871. Per the pro forma schedule, the broadband is projected to generate a profit through fiscal year 2038.

The Tennessee General Assembly has enacted legislation that authorizes local governments, including municipal energy authorities, to provide these services through their electric systems. This legislation places numerous responsibilities on local governments who determine to provide such services, including the following:

- A. A separate accounting and record-keeping system must be maintained for the operation of the electric system's internet services program. All costs, both direct and indirect, incurred in the operation of the program must be allocated to the rates charged for the services provided.
- B. An electric system cannot subsidize the activities of the internet services program by using revenues from its power operations. The only authority to use electric system funds is through the lending of funds, on a temporary basis, by an electric system. An electric system must

charge interest to the internet services program for any loans at a rate equal to the highest rate then earned by the electric system on its invested funds.

- C. An internet services program must adhere to the same terms/conditions provided in existing power pole attachment agreements, including cost allocations for rates, insurance and other expenses normally associated with similar programs operated by private providers. The rate charged to the internet services program for pole attachments must be equal to the rate charged other franchise holders providing similar services.
- D. An electric system must provide the same response times and service quality to requests made by a private provider of similar services as it provides to the electric system's internet services program.
- E. An electric system, with respect to any internet services provided, must make tax equivalent payments as required by T.C.A § 7-52-606; however, the tax equivalent payment to be made by the electric system may not exceed the amount that would otherwise be due if it were a private provider of internet services paying ad valorem taxes.
- F. An electric system, with respect to any internet services provided, is subject to make payments to the appropriate units of government for amounts in lieu of the following taxes: excise and franchise taxes authorized by Tennessee Code Annotated, Title 67, Chapter 4, Parts 20 and 21; sales taxes authorized by Tennessee Code Annotated, Title 67, Part 6; and local privilege taxes authorized by Tennessee Code Annotated, Title 67, Chapter 4, Part 7.

The State Legislature has authorized local governments to provide these services that have historically been provided by the private sector. The Legislature has also made it clear that any costs attributable to these programs must be allocated to the rates charged for services rendered, and that none of these costs are to be subsidized by electric system revenues. This requires a significant degree of recordkeeping to ensure that all expenses are properly allocated and reported. The accounting staff of BrightRidge should be familiar with these requirements and will be responsible for maintaining these records.

The legislation stipulates that the fiscal operations of the internet services program must be included in the annual financial report of the electric system as a segment of the electric enterprise fund and must be subject to a financial and compliance audit prepared in accordance with generally accepted governmental auditing standards. The officials of BrightRidge should be familiar with the requirements that have been previously applied to their other utility system operations. The Comptroller of the Treasury, through the Division of Local Government Audit, shall be responsible for determining adherence to such audit and reporting requirements. Representatives of the Division of Local Government Audit may be contacting you and your independent auditor concerning these audits.

This constitutes the report of this office pursuant to the requirements of T.C.A § 7-52-602. If the BrightRidge Board of Directors determines to proceed with the Plan, the Board must cause to be published a notice as required by law in a newspaper of general circulation in the area to be served

which specifies the date on which the Board will conduct a public hearing concerning this project. In addition, in order to proceed with the Plan, and subsequent to the public hearing, approval must be obtained by a two-thirds (2/3) majority vote of the Board or by public referendum. If actual circumstances such as the scope of the project, cost of construction, or amount of debt issued require the BrightRidge governing body to approve revisions to this Plan prior to its final approval for compliance with T.C.A §7-56-602(a), the Plan should be resubmitted to our office for a revised feasibility determination.

Sincerely,



Sandra Thompson

Director of the Office of State and Local Finance

cc: Mr. Jim Arnette, Director, Division of Local Government Audit