

The Case for the Town of Arrowsic NOT Owning a Utility

Background:

Over the past several years, the Arrowsic Broadband Authority (ABA) has committed thousands of volunteer hours and spent hundreds of thousands of donated and State grant funds to turn the aspiration of bringing broadband connectivity to the Island into a reality. The Town, upon the signing of the Service Agreement with Axiom, will take full ownership of the network and will then, for the first time, own a utility.

With this ownership will come 100% of the repair cost exposure to any damage to the network lines (exclusive of “drops” to residents), and to the equipment serving the network, as well as the care, maintenance, and upkeep of the building housing this equipment.

For taking on 100% of the repair risk to the utility, the Town will receive 40% of the revenue that the utility generates, while its partner, with no repair risk exposure, save drop repairs, will receive 60%.

While some volunteers on the ABA Committee have strongly encouraged the Commissioners to immediately explore options for the sale of the utility to avoid exposing the Town to the potential high costs of repairs, the decision has been made to defer doing so until sometime in the future.

While a reversal of this decision is not expected, sharing the following thoughts on why a sale may make more sense for the Town remains worthwhile.

Climate Action Plan Forecast

The Town recently completed a 94 page Climate Action Plan which included an extensive section dedicated to Vulnerability and Risk Assessment. Of particular note was the following:

“More frequent and severe storms could contribute to infrastructure damage with high winds, erosion, lightning, or falling debris, which could affect the function of communication systems, broadband, electricity, and other services and pose a safety hazard for community members.”

Given the remarkable amount of time and effort by Town volunteers and consultants that went into this Plan, and that it was voted on and approved by the townspeople, it is hard to understand how the utility could have a future exempt from these stark warnings.

One suggestion has been that to address the adverse weather conditions, CMP would put in place new poles with stronger power lines that would protect those of the utility. Whether or not that is the case, it is likely that CMP will not be doing any island-wide preventative work on its power lines ahead of any damage.

In order for CMP to feel compelled to make these improvements, there will need to be extensive and comprehensive (across the Island) damage occurring – much of which will result in damage to fiber optic cables, and, therefore, high repair costs.

A Paradox for the Selectboard

As detailed in the “Climate Action Plan Forecast” section above, the Climate Action Plan anticipates that severe weather and its impact on infrastructure is on the horizon. Yet, the Town has recently agreed to serve as the insurer of the utility as the financial backstop to its exposure to these forecasted costs.

It is paradoxical that the Town can adopt and concur with the core precepts of the Climate Action Plan, and then expose its operating budget to the damages the Plan expects through insuring the Town’s utility, particularly when there is no need to own the utility in the first place.

Limited Town Resources

Arrowsic has a very constrained and limited budget. Many initiatives, needs, and programmatic aspirations have had to work with limited funds and resources. The utility, should it have potentially high repair costs, will be covered by the Town as its insurer, and be depleting the Town’s resources and borrowing capacity, taking away from these many other areas that mean so much to the community.

Is it really appropriate to have a Town-owned utility serve as a fiscal priority over the other needs of the Town, when the utility’s services can be as effectively offered through a sale to a third party?

Scarcity of Volunteers

Arrowsic has a challenge with securing enough volunteers to meet all of the committee needs of the Town, so much so that the Select Board has talked about the consequences of being “under-volunteered” leading to potentially having to become a part of the Bath governmental system.

In addition to the Select Board’s time, the utility takes up the valuable time of a minimum of three and as high as eight volunteers, drawing them away from other roles they could play for the Town. So while there is a potential financial drain presented by owning a utility, there is also a clear talent drain.

Data Collection

A case has been made for waiting for a period of time before making a sale decision in order to gather more data. Whether the weather is good or bad during this waiting period, at its conclusion the Town will not know anything about the subsequent years’ weather forecast. Deferring a sale to get more data will not inform the Town about the vagaries of the following year’s weather, nor the years after.

Loss of Value

Getting maximum value for a utility is achieved when it shows positive cash flow and is profitable. The utility's financials after a year may reflect these outcomes, but it may also reflect losses and obviate the exposure to wind, ice storm and rain damage. If it is the latter, the Town will then be trying to sell an entity that has illustrated its vulnerabilities and has operated at a loss. The Town is then left with fewer buyers and certainly lower offerings – and left to retain an asset with depleted reserves that will continue to leave the Town exposed to the costs of future weather-related repairs.

This loss of value will not occur if the utility is sold early in its first year. The potential added value, if it has little to no damage in the first year, is small enough to certainly not be worth the risk. Essentially, there is limited upside, and clearly significant downside to deferring a sale.

Details of a Sale

In considering a sale, the objections raised include:

- Inability to find a provider at the start of the ABA initiative. Now that the utility is in place, there may be a good number of prospective interested parties.
- MCA Agreement expecting a return of funds - which is not the case, and
- The donor being upset about not using the funds appropriately. This concern is addressed in the “Donor Stewardship” and “Endowed Rate Protection Fund” sections below.

Potential Terms of the Utility Sale:

- Price Range: \$375,000 - \$525,000.
- 100% of all subscription fees go to Buyer.
- All repair costs to the network paid by the Buyer.
- All equipment costs (operating and replacement) paid by the Buyer.
- Buyer to pay annual rent, utilities and insurance for use of Central Office space.
- Rates set for three years with subsequent increases gradually stepped up over three years to market rates.

Donor Stewardship

In the event of a sale, there is a concern that doing so would be inconsistent with the donor's wishes for the contributed funds to go toward bringing broadband to Arrowsic.

At the same time, the donor would not want to see funds put at unnecessary risk, preferring that they be applied in as broad and as impactful a manner as possible, with a commitment to long term protection.

Given the exposure to the vagaries of future weather conditions, retaining the utility puts the remainder of the gifted funds at high risk. A far more safe, enduring and meaningful usage is possible through the establishment of the “Endowed Rate Protection Fund” described below.

Endowed Rate Protection Fund

As detailed in the “Details of a Sale” section, the Town will receive \$350-\$525,000 in sales proceeds. These proceeds can then be preserved and placed in an endowed account for subscribers, the annual return on which, when distributed to subscribers, will serve as a reserve against rising rates in the years after the rate cap in the sales agreement is lifted.

Price Protection

Selling today will do a better job of protecting subscribers from price increases than retaining ownership will. Why?

There have been discussions about having to increase rates almost immediately to build a reserve to cover future losses. A sale, done properly, locks in rates for an extended period and removes any pressure to raise rates to build reserves and cover losses from escalating repair costs.

Limited Growth, Competing Technologies

The key to the financial well-being of the utility is customer subscriptions. With an impressive 192 (approximately) initial subscribers, the Town has far outperformed expectations. That said, there is limited growth potential with about 235-240 being a maximum, offering a modest increase in revenue annually. With this small # of subscribers, the utility has an exposure to any level of attrition.

This attrition can come from the increasing efficacy of competing technologies. While these competitors are not on par with the speeds the utility can offer today, Star-link, Verizon and T-Mobile are aggressively pursuing the residential web market as a prime growth area. A small migration to these options, particularly with price sensitive customers, will have a draining impact on the utility’s finances.

By way of example, it was not that long ago that schools, colleges and universities spent millions “wiring” their campuses, only to find just a few short years later with the advancement in technology, that the wireless systems were far more impactful and certainly less costly. Quite an example to consider when operating a utility built on a network of cables.

Risk Profile: Individual vs. a Utility

Running a utility requires objectivity and looking at a decision not through one’s own lenses but through that of a Town. While it is hard to do so, it is essential to refrain from applying one’s own comfort level with risk to that of the utility, for it is not the individual taking the risk, but instead it is the Town and all its citizens.

Conclusion – A Townwide Vote

The Town has had great success bringing a vision to life, a vision that will bring higher quality of life to all of its residents on so many levels. It is a remarkable achievement.

In crafting this vision, one that forecasted not only a delivery of high speed internet service to those living throughout the Island but also a degree of profitability made possible in part due to insurance policy protection, the “crafters” did not anticipate (nor could they have) the loss of that insurance.

Today, the reality is that the utility the Town created must bear essentially all repair costs, an amount which no one can predict. The fact that insurers will not provide policies, or do so at nonsensical levels, affirms the risk that the Town is now taking on.

To date, very few well-grounded reasons for retaining ownership and for not looking for a partner to own and run the utility have been offered. Clear objections to the plan to retain ownership have not been offset by compelling rationales for said ownership.

Consider this wide range of reasons for a sale:

- consistency with the Town’s Climate Action Plan,
- subscriber rate protection,
- management of the Town’s operating budget,
- freeing up of volunteers,
- honoring the donor’s wishes,
- maximizing the utility’s value, and
- precluding subscriber erosion from advancements of competing technologies.

It is highly recommended that the Town move forward with the exploration of selling the utility, and not choose to simply let time pass until a series of weather events compel it, too late, to believe that the time is right. It will have spent reserves, lost value and narrowed the pool of prospective buyers. Retention is simply not a wise business decision, and one that should only be made with the vote of the Arrowsic community.

In a Town where a townwide vote is required on all Warrants for allocating funds as low as \$100 to a Committee, it is difficult to understand the justification for the potential allocation of thousands of dollars to its utility without a vote, a coverage that was never proposed when the ABA was established, and is in stark contrast to the projections provided at that time.

It will be unfortunate if, because of its insurance exposure, the Town has to sell assets or issue debt to cover costs, particularly without having given the citizens a chance to vote on the exposure that owning the utility created.

ABA leadership needs to not assume it can decide whether a sale is in order. Its charge was to launch the ABA, which it has done very well, but also had to do so with an unavoidable, new financial exposure to the Town, an exposure that was not part of any representation made to those who initially voted in favor of it.

In Arrowsic, when the Planning Board issues a permit and the recipient is unable to proceed in accordance with what is specified in the approved application, it asks the recipient to submit another application with the new situation to be approved before proceeding with the project.

Similarly, the Town should be asked to vote on the whether to proceed with owning the utility given that the budget and structure of what was originally approved turned out to not be feasible.

Let the townspeople decide if they want to be in both the utility and the insurance business at the same time – a combination rarely seen in business. If they vote in favor of the exposure, then all countervailing arguments will have to be put aside. If not, then a thoughtful, well managed sales process should follow.