

The Last Mile Program: Municipal Meeting

MBI
MASSACHUSETTS
BROADBAND INSTITUTE



December 14, 2015

CONNECTING THE COMMONWEALTH
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Meeting Goals

- Follow-up on December 1st statement with information, including operating agreement and business plan reviews.
- Discuss a path forward, including next steps and possible elements of a viable regional network solution
- Listen and answer questions from municipal leaders

Meeting Goals

The MBI is committed to the construction of Last Mile broadband solutions for unserved towns. We have an obligation to manage state funds effectively and support sustainable projects.

We have preference for a regional network solution and are convinced **there are viable pathways forward for regional network operations for interested towns.**

Meeting Agenda

Moderator: Phil Holahan, MassTech General Counsel & Deputy Executive Director

- **Overview:** Eric Nakajima, MBI Director [*5 minutes*]
- **Discussion on draft Operating Agreement:** Greg Sandomirsky, Mintz Levin [*15 minutes*]
- **Discussion on draft Business Plan:** Michael Morgenstern, Wipro [*15 minutes*]
- **Comments from WiredWest** [*15 minutes*]
- **A Path Forward:** Eric Nakajima & Phil Holahan [*5 minutes*]
- **Questions/Comments from Municipal Officials**
- **Questions/Comments from Additional Attendees**

WiredWest Proposal Evaluation

- MassTech/MBI staff and expert consultants met directly with WiredWest to support WiredWest proposal development more than 22 times during the past year.
- Business Plan draft shared Summer 2015, Operating Agreement drafts shared October/November 2015
- **Proposal Review Process:**
 - MBI engaged Mintz Levin to evaluate draft Operating Agreement
 - MBI engaged Wipro to evaluate draft Business Plan (with additional expert support)
 - MBI asked these experts to review proposal elements for consistency with state policy guidelines, viability of the model to be successful and sustainable, and level of financial risk to the state and participating towns.

Program Policies

- The MBI will manage project design & construction on behalf of towns, optimizing construction efficiency and achieving cost savings through aggregation.
- **The MBI will in no circumstances constrain the ability of participating municipalities from operating independently, through a cooperative or through inter-municipal agreements with other municipalities in the future.**
- Networks built by or with the support of MBI must leverage the Commonwealth's *MassBroadband123* middle-mile network.
- Networks built by or with the support of MBI must provide the opportunity for ubiquitous service & meet FCC standard definition for broadband.
- **Networks constructed entirely through investments by the Commonwealth and local residents will be owned by their respective municipalities.**
- **Networks built by or with the support of MBI must demonstrate financial and technical sustainability prior to the initiation of service.**
 - MBI will work with municipalities, MLPs and MLP cooperatives to provide appropriate feedback, guidance and technical assistance to develop sustainable operating plans.
 - MBI reserves the right to disallow proposed projects or suspend construction of a network if a sustainable operating plan cannot be demonstrated

WiredWest Municipal Light Plant Cooperative LLC

11/29/15 Draft Operating Agreement

Selected Discussion Points

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Overview of Plan

- An MLP Coop is a "public instrumentality" under MA law
- WW proposes to convert existing Corporation to an LLC
- Still purports to be a Coop of MLPs
- Relative Capital Contributions determine Percentage Interests
- Voting Rights and Income Distributions by Percentage Interests
- Member MLPs must contribute all Broadband Assets (including MBI grants)

Ownership of Network

- Clearly entirely in Coop
- Members have Percentage Interests
- No Broadband Assets return to MLPs on Withdrawal
- Coop free to lease, sell, encumber or otherwise dispose
- Not consistent with June MBI Policy Statement

Membership

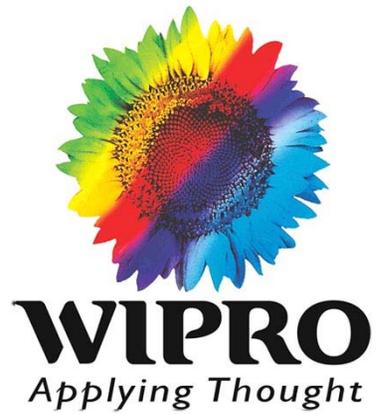
- Must Sign Up By [January 9] to be assured of entry
- Additional Members may be admitted at discretion of Initial Members
- Different Classes of Membership could be created
- Withdrawal allowed only after 10 years
- Withdrawal subject to third party contractual constraints
- Withdrawing Members get back net Capital Account (or a Note)

Capital Contributions/Financing

- Upfront Commitment from Initial Members in installments
- Additional Capital Contributions adjust Percentage Interests (but not operating revenues generated)
- Additional Capital Contributions are Not mandatory
- Most likely Source for additional funds may be borrowing
- Any Lender likely to require asset liens

Governance

- Multi-tier structure with Representatives, Directors, Executive Committee and Officers
- Compensation permitted for Executive Committee and Officers
- Private non-profit type policy on conflicts
- Executive staff led by GM
- Anticipates reliance on Public Records and Open Meeting law exemptions



Business Plan Analysis



MBI engaged Wipro to deeply analyze the public documents provided by WiredWest

Business Plan Review

Wipro was hired to consolidate all comments and analyses into a consolidated document. Subject matter experts that provided feedback on the WW Business Plan were:

- Michael Morgenstern, Consulting Partner, Wipro (extensive communications service provider advisory experience)
- Josh Brodeur, CEO, Tilson (information technology professional services and network construction experience)
- Alan Davis, CEO, Capenet (network operation experience)
- Phil Wagschal, CEO, SLIC Communications (rural network operation experience)
- Mark Cornett, VP, SLIC Communications (rural network operation experience)
- Greg Richardson, Partner, Civitium (extensive communications service provider advisory experience)
- Peter d'Errico, Leverett Broadband Committee (launched broadband services in an unserved town in MA)
- Greg Sandomirsky, Mintz Levin (counsel to MBI)

Communications service providers deliver a wide array of business functions to their customers

Required Operator Functions

Admin	Marketing	Sign-up	Install & On-Site Support	Provision	Provide Service	Bill	Remote Support
<ul style="list-style-type: none"> • Admin & Executive Staff • Rent • Electricity • Legal • Hut electricity 	<ul style="list-style-type: none"> • Marketing Staff and Expenses 	<ul style="list-style-type: none"> • Residential and Commercial Sales Staff 	<ul style="list-style-type: none"> • Technical staff • Vehicles • Warehouse • Fuel 	<ul style="list-style-type: none"> • Line Maintenance • Insurance • Fiber Replacement • Pole rental 	<ul style="list-style-type: none"> • Customer Premise Equipment • Backhaul • MRC of Phone and Television Services 	<ul style="list-style-type: none"> • Billing and Credit card Fees 	<ul style="list-style-type: none"> • Staff • Call Center Operations

MBI has sought to clearly understand how WiredWest proposes to perform those functions

Illustrative Key Business Plan Questions

- Who will be responsible for sales and marketing? Customer onboarding?
- What mix of products/services will be offered? At what price points?
- How will those services be procured?
- How will installations and break-fix be accomplished?
- What experiences lend themselves to the existing team profitably building functions from scratch versus procuring them from other vendors?
- What proof points can be provided to suggest a reasonable forecast of future customers (take-rates)?

Wipro has worked with other subject matter experts to evaluate the operational elements of the Wired West business plan

Review of the WiredWest Business Plan

Ownership of Network by WW

- WiredWest continues to assert that it will own the network instead of towns, in conflict with stated MBI program policy governing state funds

Management / Operational Costs

- A substantive number of operational cost omissions result in unrealistically favorable outcomes, such as staffing, office space, insurance, etc.
- Many start-up costs are not included, and there is no mechanism contemplated for funding start-up costs

Product Pricing

- Product pricing based on competitive markets and substantively too low to support the small scale
- Product pricing alone makes break-even almost impossible

Market Penetration Assumption

- The business plan fails to properly account for seasonal home ownership (specifically it underestimates the seasonality and overestimates the number of months homeowners will subscribe)

Product Mix/Revenue Assumptions

- High-speed subscriptions assumptions are too high

WiredWest claims that they will earn profits and therefore be able to pay back the interest to the towns

WiredWest Forecast (31 Towns)

WiredWest's Forecast

ARPU: \$111
Penetration: 47%
Subs: 15,000



*As distributed in
July 24, 2015
Financials
Document*



WiredWest
Net Gain:
\$0.5M/year
(including Debt
Service)

- Recently, WiredWest has been discussing a 55% take-rate rather than a 47% take-rate, but the difference does not meaningfully affect the conclusions

Note*: most of the difference between the Wipro gain and the WW loss can be attributed to tremendous over-staffing in the WW model

With two substantive corrections, WiredWest's forecast turns negative

Adjusted WiredWest Forecast (31 towns)

Adjusted WiredWest Forecast

ARPU: \$111
Penetration: 92%
Subs: 15,000



Added back only
two major cost
omissions (MLP
and Set-top-box
costs)



WiredWest
Net Loss:
\$1M/year
Including debt service

- After adjusting for seasonal homes, an assumed subscriber base of 15,000 across the currently in-scope towns, implies a take rate of 92%, not 47% or 55%
- Adding back MLP costs and Set-top box costs turns the forecast unprofitable
- Many other costs are still missing from the forecast

Note*: most of the difference between the Wipro gain and the WW loss can be attributed to tremendous over-staffing in the WW model

WiredWest's model overestimates upper-tier subscriptions and misses several key costs (for which WW does count revenue)

Wipro Insourced Forecast (31 towns)

Wipro Currently Expected Case

ARPU: \$62
Penetration: 40%-60%
Subs: 6,000-9,000



*Includes MLP and
Set-top-box costs
(as well as other
omissions)*



Wipro
Net Loss:
\$6M-\$8M/year
Including debt service

- Wipro constructed an operational model based on data from comparable rural markets, which forecasts a much larger loss

Note*: most of the difference between the Wipro gain and the WW loss can be attributed to tremendous over-staffing in the WW model

Towns will have to require substantive changes to the proposed business plan to reach sustainability

Recommended Adjustments

- All business functions (including administration) will need to be outsourced to existing companies
- Towns will need to pay full interest and principal on debt and MLP costs out of their budgets
- Pricing for products will need to increase by 25%-50% minimum
- Some towns may need to consider wireless technology options

Moving Forward

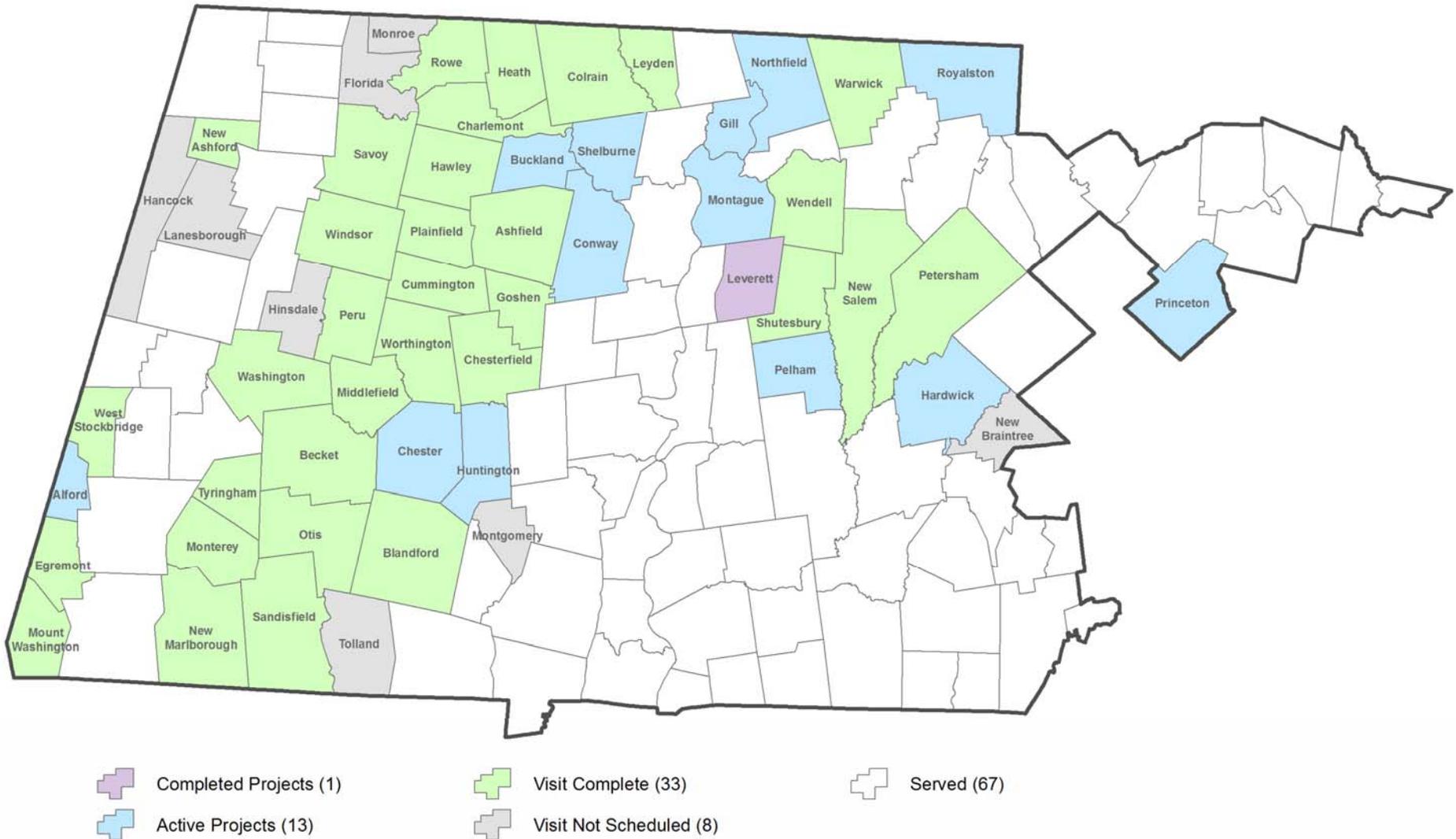
- MBI has released reviews and statement – towns and WiredWest should take time to review
- MBI & WiredWest will meet to discuss analyses and possible changes to business plan and operating agreement

Moving Forward

MBI is actively supporting Last Mile projects in many towns:

- MBI is ready to move forward with four towns – Alford, Colrain, Otis and Wendell
- MBI is engaging towns interested in wireless – Royalston, Warwick, Middlefield, Hawley
- MBI is evaluating appropriate terms for Public/Private Partnerships – especially in Petersham and Tyringham
- MBI will engage towns in consortium to advise design & construction process in early-2016

Town Engagement



For written comments or more information:

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