



Burlington Telecom, a Failing Government-Owned Network in Vermont

Burlington Telecom is a government-owned network (GON) in Vermont. Like many GONs, it is currently in dire financial straits. It also faces a lawsuit, has illegally borrowed from taxpayers, is past its deadline for completion, and has failed to attract subscribers. "In little more than a year, Burlington Telecom went from being a hopeful star of the community fiber network movement to an albatross around its neck."¹

During his campaign for office, Burlington's new mayor made fixing the network one of his primary goals. He said, "The overarching issue is putting Burlington's finances back in order. The recent financial scandals have broken the people's trust" ²

The mayor faces a daunting task.

The primary issue is the system's debt load. A state audit (the Blue Ribbon Committee) found the GON has been in violation of its state license for the five years it has been operational and that there is no feasible way that it can repay its debts.³ The system's debt totals \$51 million. As a result of this massive burden and the system's general poor financial performance, Burlington's city bond rating has been lowered three times in just two years and is now only one step above junk bond status. In its response to Moody's, the ratings service, Burlington acknowledged, "The most troubling finding of the FY11 audit was that the City has very limited liquidity. The Burlington Telecom situation is by far the largest driver of this situation ..."⁴ The reduction in the bond rating, of course, hurts the city as a whole. As noted, "Not only did the mismanaged telecom skew the city's ledgers, the financial debacle has raised Burlington's cost of borrowing."⁵

The second issue with Burlington Telecom is that \$17 million of its \$51 million debt was illegally borrowed from taxpayers. When the Vermont legislature approved Burlington Telecom, as *The Associated Press* noted, the system was required to be a "stand-alone entity" that could not "use taxpayers' money to support its operation."⁶ Also, when the state gave Burlington Telecom its charter, part of the agreement was that it would get no money from the city. However, in late 2009 when Burlington Telecom was facing financial difficulties, the previous mayor allowed the company to borrow \$17 million from the city's "cashpool," which was, by law, to be repaid in 60 days. This loan has not

¹ Mitchell, C. "Learning from Burlington," Aug. 2011.

² Ellis, C. "Trio of Candidates Compete for Mayor," *The Defender* Feb. 14, 2012.

³ Gram, D. "Vt. Telecommunications Firm not Viable, Audit Concludes," *Associated Press*, Dec. 11, 2010.

⁴ City of Burlington's Responds to Moody's Investors Service Downgrade, Press Release, June 12, 2012.

⁵ Kelley, K. "Three Years Later, Burlington Telecom is still Stuck on Pause," *Seven Days*, Sept. 9, 2012.

⁶ Gram

been - and indeed may never be - repaid. Burlington Telecom's use of these funds violated its Certificate of Public Good as well as the city's charter and Vermont state law.

The network's legal issues do not end there. Unlike other GONs, Burlington made a business decision to lease-purchase the network from Citibank. Unfortunately, "In 2010, the city council did not appropriate payments to the lease, resulting in the agreement's legal termination."⁷ Citibank claims that it is owed \$33.5 million and has attempted to repossess the equipment it financed before ultimately, deciding to file a suit against the network in federal court. The state contends Citibank could not repossess the equipment because it would result in the public utility going out of business and would therefore harm the citizens of Burlington. Burlington Telecom has an agreement with Citibank to set aside 60 percent of its net earnings to pay down its \$33.5 million debt. In July and August 2012 the combined total payment was just \$800. At that rate it will take 6,500 years to pay off the debt.⁸

Like many GONs, Burlington Telecom has also had trouble fulfilling its promises. The network has only about 4,000 subscribers, far below the number city administrators had projected. The network cannot afford to spend money on a marketing campaign so it will be difficult to increase subscribership.⁹ Furthermore, the network, which was supposed to be completed in September 2009, is only 85 percent complete. It is under state mandate to finish the network, but has no money to do so (it is estimated it will take at least \$12 million to complete) and is having difficulty raising additional funds because potential investors are reticent to get involved until the federal court rules on Citibank's suit. Even if Burlington Telecom could borrow, the state audit advised against it because it "is not practicable without exposing the City's taxpayers to a greater risk and potentially further risking the City's credit rating."¹⁰

The city is now looking for someone to buy the network, but that is also difficult given the lawsuit. The current mayor says that he does not want to spend "additional precious taxpayers' dollars gambling on the future of a telecommunications company,"¹¹ and is attempting to settle the legal dispute.¹² One also needs to question what is going to happen to the quality of the network during the ensuing legal battle. Telecommunications technologies are constantly changing and in need of continual upgrade. In this time period who will invest in these necessary changes? One would expect neither Citibank nor the city of Burlington. Furthermore, the Blue Ribbon Committee believes, "that an outright sale of BT in its current situation would not result in repaying any of the pooled cash and also would not be likely to cover the existing debt of Citi-Capital." Thus, the present net value is at most negative \$17 million. The value of the network can only decrease as the network becomes more antiquated.

Outside of a sale (and that is unlikely to recover lost revenues), it seems there is no way out of Burlington Telecom's financial troubles. Burlington Telecom has debt of \$51

⁷ Baird, J. "City to Citibank: Burlington Telecom Motion -Frivolous" Burlington Free Press, Aug. 29, 2012.

⁸ Kelley

⁹ Ibid

¹⁰ Blue Ribbon Report on Burlington Telecom to City Council, Feb. 11, 2010.

¹¹ Kelley

¹² Briggs, J. "Burlington in Mediation Talks on Telecom" Burlington Free Press, Jan. 23, 2013.

million and revenue of \$7 million. The city would need debt service totaling \$3 million to refinance \$51 million. The Blue Ribbon Committee estimates that it would need revenues to exceed \$25 million to cover the \$3 million debt service. Thus, even if Burlington Telecom could find financing, it would be spending more than 42 percent of present revenues on debt payment.

At \$51 million in debt, Burlington Telecom has failed on its basic promise - to provide universal access to residents of Burlington. There is no money to expand the network - there is not even money to market the service to potential subscribers. Burlington Telecom should heed the advice of the Blue Ribbon Committee and sell at least a majority ownership to a private firm.

If it can find a willing buyer.