October 1, 2014

Mayor Mike Amyx
City of Lawrence
6 E 6th St.
Lawrence, KS 66046

CC: Vice Mayor Jeremy Farmer, Commissioners Mike Dever, Bob Schumm and Terry Riorden, City Staff

Dear Mr. Mayor,

We have recently held very productive talks with city staff about our pending economic development request. This letter is to update you on our progress and advocate for our position on some of the policy issues that need to be decided by the City Commission.

We are in agreement with staff on the Dark Fiber Lease document. We believe that this is the best way to go and are very happy that city staff have taken the time to put this document together. It is comprehensive, well written and well thought out. It reflects substantial research on the part of city staff and will make a great model for other communities in the future. The City of Lawrence is providing leadership for other communities on this issue.

We do have some comments on the Fiber-optic administration resolution and would like to see if we can help to clarify the issues so the commission can make a policy decision.

## 1. Wicked's feels that free service under 4 (c) iii should be expanded from 100% to 140% of the net income eligible for food assistance as defined and published by the Kansas Department for Children and Families.

This would expand eligibility to more families and make the network more accessible to low income households.

## 2. Wicked's leadership feels strongly that any broadband project that receives City subsidies should be operated as a wholesale common carriage system.

What does "wholesale common carriage" mean? Simply put - any beneficiary of public subsidies must provide wholesale access to the resulting network using a non-discriminatory fee structure.

It is important to note that "wholesale" simply means wholesale access to whichever technology the operator is deploying. If that means excess fiber (as in Wicked's case) then the carrier would provide wholesale pricing for access to dark strands. If that means access to a passive optical network (PON) system, then the carrier would set up a PPPoE gateway and provide layer 2 transport for a wholesale fee.

There would be no requirements for carriers to use any one technology. The only requirements would be for the carrier to sell wholesale access at a fixed price. Every retailer would be treated the same no matter how many (or how few) drops were active.

The city would not be involved in the regulation of these wholesale agreements. The city would simply include the requirement in agreements signed with carriers who are requesting subsidies. If participating carriers were then unwilling to implement the wholesale system, other carriers would have a cause of action and the matter would be settled between them in district court.  The city would not need to be involved.

Carriers who do not want to provide common carriage service do not have to.  They would simply be ineligible for a subsidy from the city.

This approach has several substantial benefits for the City of Lawrence and its citizens:

**i. Common carriage prevents the creation of a new natural monopoly.**

Granting exclusive franchises to phone and cable companies has resulted in non-competitive markets, high prices, lack of innovation and a dearth of customer choices.  Lets not repeat the mistakes of the past.

Remember; both the telephone and cable systems were subsidized by taxpayers in the form of low interest loans and exclusive grants of access to the rights of way.  This was deemed appropriate because these industries were regulated.

Since the early 1980s the telecommunication sector has been de-regulated in the name of increasing competition and giving customers choices.  The results?  Natural monopolies and ever increasing prices.  Most communities still only have one choice for cable TV and one for landline service, but now they pay higher prices and, in some cases, are no longer able to access landline networks.

Lets not repeat this mistake.  If incumbents had been required to implement wholesale systems as a condition of the public subsidies they received, the telecommunications landscape would look much different today.

**ii. Common carriage prevents wasteful use of the rights of way.**

If every telecommunications carrier has to build a separate network, then a city with robust competition would end up looking like this:

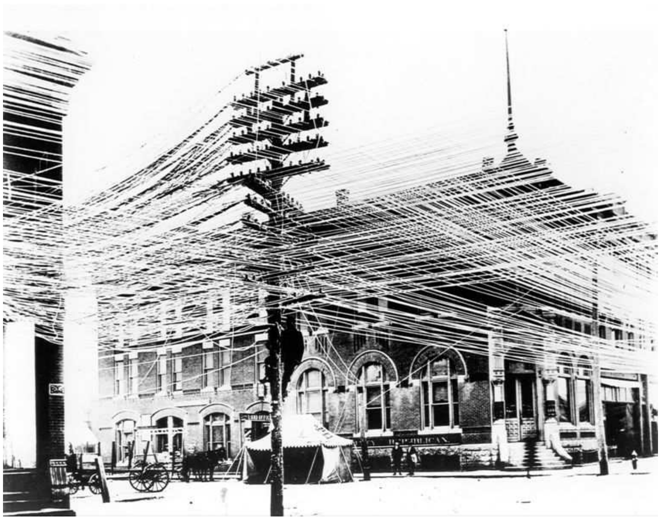

**Figure 1: Pratt Kansas Telephone Wires - 1912**

In much the same way that the municipality requires telecommunications and electricity providers to share poles, the municipality has an interest in preventing the rights-of-way from being cluttered with multiple overlapping networks - both aerial and underground.

**iii Common carriage reduces the amount of investment necessary to have a competitive marketplace.**

This is one of the key reasons for requiring common carriage.

Certain areas of the city will be more profitable for carriers than others (downtown for example). Unless there is a common carriage requirement, there is a strong possibility that multiple carriers will request subsidies to build out the same neighborhoods.

This is already happening. Wicked first proposed installing a fiber network in downtown Lawrence more than a year ago. Since then *The Reflective Group Llc/Dawn Fiber, Llc DBA Freestate Broadband/RG Fiber* has indicated that, with public subsidies, they also want to build out a fiber to the home system in this neighborhood.

Should *The Reflective Group Llc./Dawn Fiber, Llc DBA Freestate Broadband/RG Fiber* secure the necessary funding and expertise, the City would be in danger of subsidizing multiple fiber providers in downtown Lawrence, but have none in other neighborhoods that might benefit from fiber-optic services.


**Figure 2: Wicked Pilot Area (Self Selected)**


**Figure 3: The Reflective Group Llc/Dawn Fiber, Llc. DBA Freestate Broadband/RG Fiber Pilot Area**

Requiring subsidy recipients to operate as wholesale common carriers would prevent duplication of effort. It gives a strong incentive for potential operators to work together and focus their resources on adjacent neighborhoods, then provide reciprocity through wholesale agreements.

This leverages the investments of competing carriers to encourage a build-out that will some day cover the entire community.

**iv. The City of Lawrence should be highly suspicious of any operator who wants both public incentives and exclusivity.**

If the city is being asked to subsidize a network system, it should require the operator to act in the best interests of the public.  That means encouraging robust competition not creating exclusive systems where operators can charge exorbitant rates for sub-par service ( we already have two of those ).

Any operator who wants exclusivity is not planning on operating for the benefit of the public, they are planning to operate for the benefit of their personal pocketbook.

If operators want exclusive access to infrastructure, they should fund it exclusively with their own funds.

**v. Wicked has proposed specific criteria for wholesale pricing.  We are willing to abide by it and would encourage the City to adopt it across the board for any ISP who wants to access public subsidies under section 4 (c) iii. of the proposed ordinance.**

The following would be for 1 Gigabit service from a customer premises to the nearest point of presence. From that point, carriers would be responsible for carrying traffic back to the Internet on their own infrastructure or infrastructure leased from the City or other willing participants.

Prices to be fixed as follows in 2014 dollars and adjusted annually based on the consumer price index as published by the Bureau of Labor Statistics

- Monthly wholesale cost - $25.00 per month per drop
- Activation fee - $50.00 per drop
- Minimum wholesale order - 100 drops
- Maximum deposit required - 3 months
- Any price increases in excess of the agreed pricing would require approval from the City Commission

## 3. Wicked's leadership feels that direct subsidies to carriers in the form of a loan guarantee, loans or grants should require the payment of a 5% fee on gross revenue.

Economic Development incentives to real-estate projects in our community can be justified through growth in future taxes.  By increasing the value of a property, the assessed taxes go up.  At the end of the incentive period, the taxpayers benefit through a larger tax base.

Since broadband is exempt from sales tax and municipalities are prohibited from charging franchise fees on broadband services, investments to expand broadband access will not automatically increase the municipal tax base.

To address this issue and encourage both the City of Lawrence and other municipalities to participate in programs to expand broadband, Wicked believes that the payment of a 5% fee on gross revenue would be beneficial to both the company and the City of Lawrence.

Wicked proposes that any direct subsidy in the form of grants, loans, loan guarantees or in-kind cooperation stipulate that the recipient pay a 5% fee on gross revenue.  This is not a franchise fee, but a quid-pro-quo return on the City's investment.

Finally, Wicked would like to comment on the financial incentives package that has been requested and recommended by both PIRC and the RFI Review Committee.

The waiver of the first $20K in rental fees is important because it offsets the costs of what has now been an extended proposal and review process. Wicked has spent a large sum of money communicating to the public the benefits of ultra-high speed broadband and will continue to invest these monies in network improvements and expanded fiber access. Since this rental fee is paid voluntarily, Wicked believes a waiver of the first $20K each year for 5 years as part of a larger incentives package is reasonable.

The final item is the $1 Million loan guarantee. As we've said before, this project is not possible without some form of financial incentive from the City of Lawrence. This guarantee is necessary for the following reasons:

- All projects of this type require extensive involvement from municipalities. To create a financially sustainable network takes either a massive investment of capital and national scale (Google Fiber) or participation from taxpayers (Longmont Colorado, Chanute Kansas, Chattanooga Tennessee, Lafayette Louisiana)
- Financial viability requires low interest rates and long payment terms (patient capital). Without city participation, no fiber project will be viable (i.e. project meets “but for” threshold).
- Banks do not collateralize network projects in the same way they do real estate. Similarly, banks do not collateralize roads, electrical grids, or water and sewage projects.
- Post 2008, banks always seek to achieve a collateral position greater than 100% on a loan, unless the loan is government backed.
- Equity investors are concerned about investing in Lawrence without participation from the City.
- When successfully implemented, this approach sets a precedent for other communities to help fund CWC’s expansion in the same way. This paves a path for a Lawrence-based business to expand to surrounding cities.

In consultation with staff, Wicked is willing to scale back its pilot project to around 300 addresses. This scales back the company's loan guarontee requirement to $300K. Implementing a pilot on this smaller scale will help to prove the viability of the project and allow Wicked to pursue new equity investment with a firm demonstration of support from the City of Lawrence.

Once the pilot is complete, the issue of the remaining $700K can be addressed. It may be unnecessary if the company is successful in pursuing equity partners or crowd funding resources. Regardless, scaling the initial pilot back will reduce the city's risk while allowing the project to move forward immediately.

Sincerely,

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