

MUNICIPAL BROADBAND FINANCING IN TENNESSEE

July 19, 2023

OBJECTIVES

- Brief overview of municipal broadband statutes in Tennessee
- Examples of municipal broadband providers in Tennessee
- Introduction to municipal energy authorities
- Municipal broadband financing options
- Federal tax issues related to municipal broadband financing
- Tax incentives for private broadband providers
- Meet the Bass, Berry & Sims Public Finance Team

MUNICIPAL BROADBAND STATUTES IN TENNESSEE

- Tennessee's municipal broadband statutes have not been amended since 2004 and 2008.
- In 2015, there were 19 states, including Tennessee, that either banned or restricted municipal broadband services.
- Broadband has more recently been viewed as an essential service.
- Tennessee law restricts the provision of municipal broadband services to the following:
 - Municipal Electric Utility Providers
 - Telecommunications Joint Ventures

MUNICIPAL BROADBAND STATUTES IN TENNESSEE

Municipal Electric Utility Providers, including Energy Authorities, must comply with the following requirements prior to establishing a Municipal Broadband Division:

Service Area Limitations

- Within or without the corporate or county limits of such municipality, and, with the consent of such other municipality, within the corporate or county limits of any other municipality.
- Municipalities shall not have any power or authority to provide broadband in any area where a privately-held cable television operator is providing cable service over a cable system and in total serves six thousand (6,000) or fewer subscribers over one (1) or more cable systems.
- Municipalities shall not have any power or authority to provide broadband in any area of any existing telephone cooperative that has been providing cable service for not less than ten (10) years under the authority of the federal communications commission.

Transparency Requirements

- Upon the approval and at the direction of the governing board, the municipal electric system shall file a detailed business plan with the office of the comptroller of the treasury that includes a three-year cost benefit analysis and that identifies and discloses the total projected direct cost and indirect cost of and revenues to be derived from providing the proposed services. The plan shall also include a description of the quality and level of services to be provided, pro forma financial statements, a detailed financing plan, marketing plan, rate structure and any other information requested by the comptroller of the treasury.

MUNICIPAL BROADBAND STATUTES IN TENNESSEE

Transparency Requirements

- Municipal system shall publish, in a newspaper of general circulation within that area, a notice of its intent to proceed with the offering of additional services. The notice shall include a general description of the business plan and a summary of the governing board's findings on such plan. The notice shall also specify a date on which the governing board shall conduct a public hearing on the provision of such services
- The governing board shall conduct a public hearing on the provision of such services. No sooner than fourteen (14) days after such public hearing, the governing board may consider authorizing the provision of additional services. A municipal electric system may provide additional services only after approval by a two-thirds (2/3) majority vote of the chief legislative body of the municipality in which the municipal electric system is located or by a public referendum

The establishment of a Telecommunications Joint Venture requires the following:

- Any municipality or county government seeking to establish a joint venture shall apply to the Tennessee Public Utility Commission (TPUC) for a finding that the area is historically unserved and that no private provider intends to serve that area. The applicant shall provide a copy of the application to all telecommunications providers offering service in the area applied for and to all holders of state-issued certificates of franchise authority or local franchises in areas within fifty (50) miles of the area applied for at the same time it submits its application to TPUC. The application shall include proof that the municipality or county has publicly advertised its intent to establish a joint venture to provide service. The municipality or county shall demonstrate that it has provided notice of its intent to all area broadband providers at least sixty (60) days prior to its submission of its application to TPUC. All area broadband providers shall have the right to submit comments regarding any application to the TPUC. All records of a telecommunications joint venture shall be available for disclosure and public inspection pursuant to title 10, chapter 7. All meetings of or pertaining to a telecommunications joint venture shall be open meetings in accordance with title 8, chapter 44.

MUNICIPAL BROADBAND PROVIDERS

- **East Tennessee:**
 - Athens Utility Board
 - BrightRidge Broadband
 - Bristol TN Essential Services
 - EPB Chattanooga
 - City of Maryville
 - Erwin Utilities
 - Lenoir City Utilities Board
 - Newport Utilities
 - Knoxville Utilities Board (in process)
 - Cleveland (in process)



MUNICIPAL BROADBAND PROVIDERS

- **Middle TN:**

- CDE Lightband – City of Clarksville
- CPWS Broadband – City of Columbia
- Fayetteville Public Utilities
- PES Energize – City of Pulaski
- Tullahoma Utilities Board
- Dickson (in process)

- **West TN:**

- Jackson Energy Authority
- Milan Public Utilities
- Lexington (in process)



MUNICIPAL ENERGY AUTHORITIES

- “Associated municipality” means a municipality that is located in any county other than Hamilton, Knox, Davidson, or Shelby, and, as of the date an authority is formed, operates an electric system under the authority of chapter 52 of title 7; the municipality's charter; or otherwise applicable law. See Tenn. Code Ann. § 7-36-102.
- If the governing body of an associated municipality, by appropriate resolution, duly adopted by a two-thirds ($\frac{2}{3}$) or greater vote, finds and determines that it is wise, expedient, necessary, or advisable that an authority be formed, it shall authorize the mayor of the associated municipality or other person to proceed to form an authority, and shall approve the form of certificate of incorporation proposed to be used in organizing the authority, and then the mayor or other person authorized by the resolution shall execute, acknowledge, and file a certificate of incorporation for the corporation.
- Maintain within or outside the corporate limits of the associated municipality, a system for the furnishing of electrical, water, wastewater, or broadband services.
- Board members subject to approval of governing body—flexibility to determine process for appointment in incorporation documents.

MUNICIPAL ENERGY AUTHORITIES

- ◆ Bolivar Energy Authority
- ◆ BrightRidge
- ◆ Brownsville Energy Authority (private act)
- ◆ Cleveland (in process)
- ◆ Erwin Utilities authority
- ◆ Greeneville Energy Authority
- ◆ Jackson Energy Authority (private act)
- ◆ Jellico Utilities Authority
- ◆ Paris Utility Authority
- ◆ Tullahoma Utilities Authority (private act)
- ◆ Union City Energy Authority



MUNICIPAL BROADBAND FINANCING OPTIONS

Financial Needs

- ❖ Capital assets to be jointly used with electric operations (e.g. backbone fiber infrastructure)
- ❖ Capital assets to be exclusively used in broadband operations
- ❖ Broadband working capital (e.g. salaries, marketing, telecom product and other operating expenses allocable to broadband)

MUNICIPAL BROADBAND FINANCING OPTIONS

- ❖ City general obligation bonds (broadband revenue and tax bonds)
 - Stronger credit, thus lower interest rates and debt service
 - Need strong political/public buy-in
- ❖ Electric system revenue bonds
 - Stronger credit, thus lower interest rates and debt service
 - Cost-sharing
- ❖ Broadband revenue bonds/lines-of-credit
 - During start-up phase, limited market for this type of debt
 - Weaker credit, thus higher rates and debt service
- ❖ Interdivision loan from electric system
 - Rate = at least maximum rate on electric investments
 - Limited to available electric reserves

MUNICIPAL BROADBAND FINANCING OPTIONS

❖ Working capital

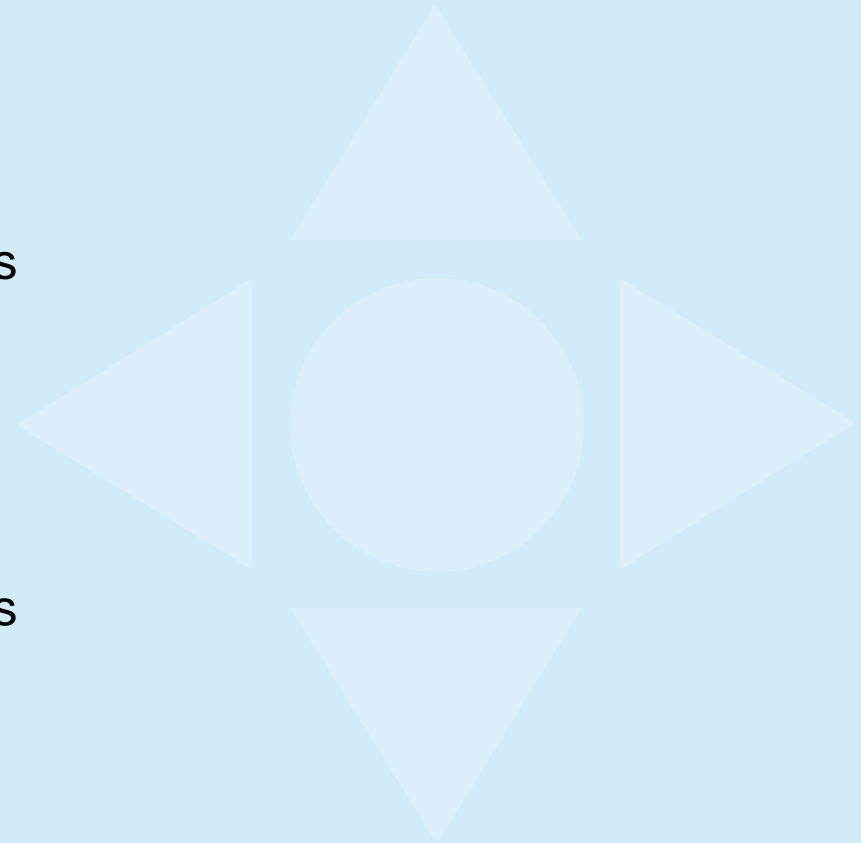
- Interfund loan
- Broadband revenue line of credit

❖ Broadband-exclusive assets

- Interfund loan
- City-backed broadband revenue and tax bonds
- Broadband revenue bonds/line of credit

❖ Joint-use assets

- Interfund loan
- City-backed broadband revenue and tax bonds
- Broadband revenue bonds
- Electric revenue bonds



MUNICIPAL BROADBAND FINANCING OPTIONS

- ❖ Electric system prohibited from subsidizing broadband system
 - Separate divisions
 - Broadband division must pay electric division for use of electric system assets, and vice versa
 - Electric division may not pledge its revenues to secure debt for capital assets that have no bona fide use in the electric division
 - Interdivision loans must bear interest at maximum rate being earned by electric division investments
- ❖ Long-term bonds generally restricted to capital improvements
- ❖ TVA Requirements regarding use of electric funds/assets

MUNICIPAL BROADBAND FINANCING OPTIONS

- ❖ Two funding sources
 - Public market bond offering
 - Bank loan
- ❖ Strong preference for established revenue streams sufficient to support debt payments
- ❖ Debt can also be secured by pledge of broadband equipment
- ❖ During initial start-up, obtaining credit may be difficult
- ❖ Until operations have stabilized, bank loan is likely more feasible

FEDERAL TAX ISSUES

- Tax-Exempt Bonds – federal subsidy of local government activities
- Subsidized facilities not to be used for private activity, which requires both:
 - Private Use - use in the trade or business of a nongovernmental entity on a basis not available to the general public and
 - Private Payment – payments related to the use are available to pay debt service on the bonds
- Nongovernmental entity means any entity that is not a state or local governmental entity
 - Includes non-governmental non-profit entities
 - 501(c)(3) entities have separate authority to obtain benefits of tax-exempt bonds
 - Includes the federal government and its agencies and instrumentalities

FEDERAL TAX ISSUES

- Private Activity
 - Municipality issues \$10 million of tax-exempt bonds to fund construction of a new municipal utility administrative facility. Utility needs only half of the space and leases the remainder to a local bank in exchange for rent equal to $\frac{1}{2}$ of the debt service on the bonds. Includes private use and private payment.
- Not Private Activity
 - Municipality issues \$10 million of tax-exempt bonds to fund construction of a new electric substation. Local bank is a customer of the electric system (paying scheduled rates) and uses the System's electric services in its business. No private activity because those services are available on the same basis (even if on a different portion of the rate schedule) to the general public.

FEDERAL TAX ISSUES

- Types of Private Use
 - Ownership
 - Leasehold interest
 - Management or service agreement that:
 - gives the service provider an ownership or leasehold-type interest in the managed property
 - provides for compensation for services based, in whole or in part, on a share of net profits from the operation of the facility
 - Other contracts/agreements that convey special legal entitlements
 - Other arrangement that doesn't benefit general public and provides special economic benefit to a nongovernmental person

TAX INCENTIVES FOR PRIVATE BROADBAND PROVIDERS

- ❖ PILOT - Property tax abatement known as a “payment in lieu of tax” agreement.
- ❖ TIF - Diversion of incremental property taxes to pay or finance project costs known as a “tax increment financing”.
- ❖ Sales taxes are not affected.
- ❖ The industrial development board statute defines “projects” to include many types of capital improvements, both public and private. (Tenn. Code Ann. § 7-53-101(15)).

TAX INCENTIVES FOR PRIVATE BROADBAND PROVIDERS

- ❖ Most relevant to private broadband providers, “Project” means any land and building, including office building, any facility or other improvement on the land, and all real and personal properties deemed necessary in connection therewith, whether or not now in existence, that shall be suitable for the following:
 - Any commercial enterprise in selling, providing, or handling any financial service or in storing, warehousing, distributing or selling any products of agriculture, mining or industry.
 - All or any part of any office building or buildings for the use of such tenant or tenants as may be determined or authorized by the board of directors of the corporation, including, without limitation, any industrial, commercial, financial or service enterprise, any nonprofit domestic corporation or enterprise now or hereafter organized, whose purpose is the promotion, support and encouragement of either agriculture or commerce in this state or whose purpose is the promoting of the health, welfare and safety of the citizens of the state.

PUBLIC FINANCE TEAM



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