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Chattanooga residents get Internet, courtesy of taxpayers

By [TNWatchdog Staff](#) / December 21, 2011 / News / [No Comments](#)



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By CHRISTOPHER BUTLER

Some people believe the Internet is entertainment, a form of recreation.

Others, meanwhile, believe it is a vital piece of infrastructure, something society can no more do without than roads, law enforcement, or even basic sewer systems — and one that requires government intervention.

Chattanooga Electric Power Board (EPB) President & CEO Harold DePriest belongs to the latter category.

“The issue is whether you think this is just entertainment or whether you think this is infrastructure that benefits the public,” DePriest told *Tennessee Watchdog*.

When asked, an EPB official said government has a responsibility to help provide not only basic Internet as infrastructure, the same way it offers electricity — but, in addition, something known as ultra-high speed Internet, which few people in the world even have.

Officials who work in the private telecommunications business said the demand for this type of Internet, which reportedly runs almost 200 times faster than what most people currently have, is many years away (only Hong Kong and a few other cities throughout the world offer the service). EPB’s telecommunications service is called EPB Fiber Optics. Some facts about EPB Fiber Optics:

- EPB Fiber Optics is a separate entity from the public company’s basic utility service.
- The entity charges around \$50 a month for its basic Internet.

• EPB Fiber Optics also charges seven times as much (\$350) to those who wish to pay for its ultra-high speed service — which only a handful of Chattanooga residents thus far want.

EPB cannot offer the ultra-high speed Internet without an enhanced electrical system known as a Smart Grid. EPB officials say their primary purpose in installing the Smart Grid/fiber optic network is to offer better electrical service, which includes the ability to monitor electricity levels at customers' homes using smart meters — even though DePriest admitted last month they could get the same information, and with the same accuracy, without the Smart Grid.

The Smart Grid's total cost — more than \$300 million. \$111 million of that money came courtesy of taxpayers, via federal stimulus money. Customers who only use EPB's electrical service are responsible for financing \$160 million via a loan to EBP Telecom, while EPB's actual Internet and cable television customers are responsible for the remainder.

Naturally, private competitors are unhappy.

Ask DePriest, however, and he said most Chattanooga residents remain unconcerned, just as long as they get good Internet.

Harold DePriest on EPB Fiber Optics



[YouTube](https://www.youtube.com/watch?v=fVTnjGc-j7k) (<https://www.youtube.com/watch?v=fVTnjGc-j7k>)

(DePriest spoke to *Tennessee Watchdog* in this [exclusive video](https://youtu.be/fVTnjGc-j7k) (<https://youtu.be/fVTnjGc-j7k>))

“To tell you the truth, my customers don't care as long as they get good services at a good price,” DePriest (seen in [this video](https://www.youtube.com/watch?v=oRtzmNMGILo) (<https://www.youtube.com/watch?v=oRtzmNMGILo>)) discussing EPB broadband before state legislators) said.

“When we got in business, Chattanooga had 20 High Definition channels. Today we have 120. When we got in business we had exceedingly

slow Internet, but now we've got one gigabyte.”

In fact, EPB is one of nine publicly-owned communications networks in Tennessee.

According to a recently published study, since the time they were created, those nine publicly-owned communications networks have accumulated a deficit of \$176 million.

Most government-owned communications networks, however, do not make profits the same way a private business would, said Ronald Rizzuto, author of the study and a professor of finance at the University of Denver.

Furthermore, anyone who believes government should make this service available has not yet realized something, Rizzuto told *Tennessee Watchdog*.

“Obviously, the Internet has become a critical asset for any business, but, by the same token, what about private rights? This is like saying McDonalds hamburgers are a necessity so government-run entities must offer hamburger stands to compete. At the same time, there is the whole private infrastructure that they are competing against.”

‘BECAUSE WE CAN’

In his report, Rizzuto did not have to cite a specific government-owned communications system that once operated out of Memphis — that is because, as economists had warned would happen as early as 11 years ago, it made no profits and ceased to exist.

(<http://tennessee.watchdog.org/file>

Ron.jpg)

Ron Rizzuto

According to the Oct. 13, 2000 edition of the *Memphis Commercial Appeal*, economists warned officials that Memphis Networx, owned by the Memphis Light, Gas and Water Division and financed by Shelby County ratepayers, would fail (the failure of which is documented in [this video](https://www.youtube.com/watch?v=YH3S8LPFY5k) (<https://www.youtube.com/watch?v=YH3S8LPFY5k>)).

The failure of Memphis Networx did not deter other government entities throughout Tennessee from introducing their own communications systems to compete with the free market.

In addition to EPB Fiber Optics, entities include those in the following areas:

- Bristol
- Clarksville
- Columbia
- Fayetteville
- Jackson
- Morristown
- Pulaski
- Tullahoma

Despite the failure in Memphis, and despite complaints from officials in the telecommunications industry that government has no place competing with the private sector, DePriest expanded EPB in 2007 from an electricity business into a telephone, cable TV, and high-speed broadband Internet service.

Using stimulus money and a tax-exempt bond financed expansion program (much of which EPB electricity ratepayers were responsible for funding), EPB said it established its fiber optic network, primarily to improve services for electrical customers. For secondary purposes, EPB said it used the fiber network as a tool to help the entity expand into the largest municipal utility in the nation to offer telecommunications services.

As stated at the time, EPB wanted its new telecommunications division, still a government-run entity, to take at least 35 to 50 percent of the cable TV, telephone and high-speed Internet market from the private entity Comcast, the primary provider of such services in Chattanooga.

At the time DePriest complained publicly that current telecommunications providers offered poor service and needed competition.

The Chattanooga City Council later approved EPB's plan, by a unanimous vote.

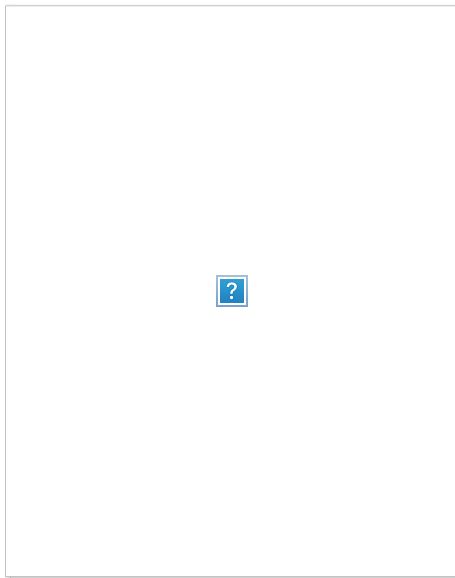
As for the \$350 ultra-fast Internet, DePriest told the *New York Times* last year that he did not know if \$350 was the proper amount EPB should charge for such a service.

"We don't know how to price a gig. We're experimenting. We'll learn," DePriest said.

The *New York Times* then asked DePriest why EPB even offers the service. His answer was short and to the point:

"The simple answer is because we can."

A LACK OF DEMAND



(<http://tennessee.watchdog.org/files/2011/12/Jack-Benson.jpg>)

Jack Benson

Chattanooga City Council member Jack Benson, who voted in favor of EPB Fiber Optics, said creating the entity was necessary. Too many people in Chattanooga were displeased with Comcast's service — thus the need for a government entity to compete against a private enterprise.

"I voted for it mainly because Comcast had failed to be service friendly here in Chattanooga, and we had a number of complaints that they were hard to get a hold of. We felt like Comcast had a monopoly and that this (EPB competing against Comcast) would make both services better," Benson said.

David Snyder, who operates an Internet Service Provider in Dayton, 35 miles north of Chattanooga, and who competes for customers against EPB, disagrees with Benson's assessment.

The greater the competition among private companies in Chattanooga, the happier the consumer — but because of EPB's presence, the city offers no profit potential. Snyder and most other service providers in the area now avoid Chattanooga, he said.

Nevertheless, current technology permits Chattanooga residents to choose from multiple cable and Internet carriers — in other words, no one need worry about any one private company having a monopoly. EPB may eventually have a monopoly, regardless, because fewer and fewer private companies wish to compete against them, Snyder said.

"A lot of people (in Chattanooga) believe EPB is a private competitor who is giving Comcast and AT&T what they deserve for their poor customer service. But now there are tremendous advances in telecommunications for local competition and a lot of investment going on by private companies. AT&T competes with Comcast for television delivery services, for instance. It's a major disincentive when you have a government-subsidized competitor there. There is robust competition in this industry, and it is getting more robust by the day."

“As long as EPB is still paying off that \$200 million bond, they are not really profitable.”

Snyder has this to say about EPB’s ultra-fast Internet service:

“I have been in this business for 15 years, and I can tell you that we take bandwidth consumption very seriously. I can also tell you that no home users even need close to the amount of data that ultra high-speed Internet offers. EPB likes to say they are 10 years ahead of the curve, and that is why they needed to spend all of that money, but all they are doing is showing that their government spending is out of control.

“They have built a solution looking for a problem. It makes for great marketing, but there is no demand for this service. By the time this service is needed, the private sector will have established this for pennies on the dollar. Meanwhile, EPB spent hundreds of millions of dollars to have this before it was in demand,” Snyder said.

EPB RESPONDS

Danna Bailey, spokeswoman for EPB, rebutted the criticism.

“Other companies in the private sector were not bringing this kind of connectivity to our community, and we believe that it is critical infrastructure for economic development and, ultimately, quality of life. That’s what government’s role should be — to provide critical infrastructure for economic development and quality of life when the private sector does not.”

Bailey admitted, however, that most of EPB’s 30,000 subscribers do not use the ultra-high speed Internet and choose a more basic option.

“We have a handful of residential gigabit-per-second subscribers and nearly two dozen businesses. For some companies and individuals, this kind of connectivity is worth the money. A Mercedes Benz is out of reach for most individual families and small businesses. That doesn’t mean a Mercedes Benz shouldn’t be on the market,” Bailey said.

When asked what EPB would say to competitors who object to a government entity entering the free market to compete against them, Bailey said this:

“We believe in the free market. We also believe that it is our responsibility to provide critical infrastructure when the private sector won’t.”

The ultra-high speed Internet has helped attract at least 2,000 jobs to the Chattanooga area, she added.

At a recent meeting of the Chattanooga Tea Party, DePriest said he did not hesitate to spend stimulus money to install the Smart Grid technology, which included the ability to install smart meters, which tells EPB when power is on and off at someone’s house and remotely measure how much power is used at a house.

“I want to spend every (stimulus) dollar as quick as I can before they run out of money. That’s just the truth,” DePriest said.

Snyder, who was in the audience, asked DePriest the following, as it related to already available radio/cell phone technology that can transmit that same data back to EPB, but only at a slightly slower pace, exactly 25 minutes:

“Telephone, Internet, and cable TV aside, is there any reason to have fiber-optic cabling at the expense of \$200 million to run the Smart Grid when it could be run by cell phones?”

DePriest’s response:

“If we put in the wireless system (that you are referencing), the fastest we could read meters would be within 25 minutes. With the fiber system, we can send out the signal and get the readings within one minute. Speed is everything with these systems because what it does is give you real time data to make real time decisions with.”

At the end of that meeting, one Tea Party official stood in front of DePriest, and said EPB's acceptance of stimulus money bothered him.

"Unfortunately, EPB along with every other government official, feels like that is free money — but the taxpayers are the ones who are paying for it.

WHAT RIZZUTO SAYS

There are two primary reasons why government-run communications services are bad, Rizzuto told *Tennessee Watchdog*, when asked about his study.

"They will be the fifth competitor against private companies. They think they can go in and take market share, but it's a tough competitive environment and it takes a lot of money to be competitive.

"The other factor that contributes to the downfall of these type companies is that they don't run them like true businesses. They get these companies approved by promising citizens that rates are going to be low and they won't have rate increases — so they don't raise rates sufficient to cover costs, so they run deficits. When you look at my report, you will see that most of the entities (in Tennessee) are running deficits. They don't run them like competitive businesses."

The government-run Internet service in Fayetteville is an example of a company that runs up deficits each year, Rizzuto said.

In fact, 75-80 percent of government-run communications systems throughout the nation do not make money.

Bailey and Benson, however, question whether Rizzuto's study has merit and wonder whether the telecommunications industry paid Rizzuto to write it.

Rizzuto denies the accusation.

"I was not paid for my analyses. I have not requested nor received fees for any analysis that I have done on Tennessee's municipal overbuilds over the past 10 years. Municipal overbuilds are an area of academic research for me," Rizzuto said.

While Benson said that EPB has provided competition that is wonderful for the Chattanooga market, Snyder cautions Chattanooga consumers to remember something:

"I caution the rest of the free market in Chattanooga to watch out. What is to stop the government from getting into other businesses, like tow trucks or hotels, if they see a need?"

"I would prefer that people work as market entrepreneurs rather than government entrepreneurs."

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[MAJOR FINDINGS OF RIZZUTO STUDY "FINANCIAL PERFORMANCE OF TENNESSEE'S MUNICIPAL CABLE AND INTERNET OVERBUILDS IN 2010"](#)

- As of 2010 there were nine municipal communications operations operating in Tennessee (Bristol, Chattanooga, Clarksville, Columbia, Fayetteville, Jackson, Morristown, Pulaski, and Tullahoma), with Tullahoma, the oldest, having been in operation since 2001.

- Municipal electric utilities in Tennessee have incurred deficits of approximately \$176 million for these communications ventures, since their inception. This represents an increase of \$8.5 million over the deficit in 2009.
- In 2010, only two of those nine operations generated sufficient revenues to cover all the costs of their operations (operating, capital and debt service costs). Columbia and Jackson generated positive free cash flow. Pulaski covered all of its operating costs; however, all the capital costs and most of the debt service costs were shifted to the electric utility in 2010. The six other municipal ventures generated deficits.
- During 2010, Tennessee's municipal communications ventures required \$14.4 million in additional public debt and/or loans from sister electric utilities to cover deficits.
- Several of the communications ventures in Tennessee appear to be engaging in activities that are contrary to Tennessee law.
- Morristown and Pulaski electric utilities appear to be subsidizing their communications ventures. According to Tennessee law, the electric utility may not subsidize the operations of the communications unit with revenue from its power operations.
- Some of the electric utilities are allocating capital costs for the communication business to the electric utility rather than the communication utility. (1) The municipal utility in Bristol has invested \$50 million in fiber optic communication infrastructure, but has allocated only \$2.5 million to its communications operation. (2) The municipal utility in Chattanooga issued bonds for \$219.8 million to finance the construction of a fiber optic broadband network; however, only \$48 million of that debt was allocated to the communications business unit. This also violates Tennessee law that says "A municipal electric system providing any of the services authorized by this part shall establish and charge rates that cover all costs related to the provision of such services."



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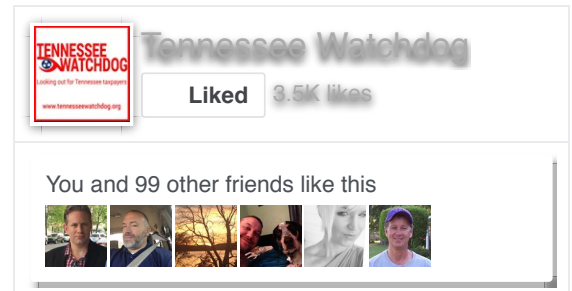
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