

## ISSUER COMMENT

## Burlington, Vermont Approves a Credit Positive Telecom Settlement

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On February 18, the [Burlington](#) Vermont (Baa3 negative) City Council approved the terms of a settlement agreement with Citibank in the two-year-old Burlington Telecom (BT) lawsuit. The council's approval is credit positive for the city, which has agreed to settle the lawsuit for about one third of the original claim. The settlement agreement establishes that the city will pay Citibank \$10.5 million, versus an original claim of \$33.5 million, plus a share of BT's future value. The settlement also outlines future actions and financial milestones to fully dismiss the lawsuit. The city expects to fund its payment largely from telecom revenues.

The city established BT in 2005 as an enterprise to provide broadband cable service. In 2011, Citibank filed a lawsuit against the city for unpaid portions of a lease-purchase agreement that the bank had extended to the city in 2007 to create the enterprise system. The broadband service did not meet revenue targets which led to the termination of the agreement.

The city's expects its \$10.5 million settlement payment to Citibank to come from multiple sources, as described in the exhibit below. Although the city intends for the payment to be made from telecom revenues and not to be supported by taxpayers through the city's general fund, the city has yet to identify about 70% of the financing sources.

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**Burlington, Vermont, Funding Sources for Its \$10.5 Million Settlement Payment to Citibank**

Amount	Source	Status of Funds
\$6,000,000	Bridge financing from special situation lender	To be determined
\$1,469,000	Co-defendant law firm and/or its insurance carrier	Insurance / Private payment
\$1,300,000	City of Burlington payment	To be determined
\$981,000	Burlington Telecom revenues paid to Citibank	Court escrow account
\$500,000	City of Burlington's insurance carrier	Insurance
\$250,000	Burlington Telecom additional revenue payments	Paid between now and closing of settlement

Source: Mediated Settlement Agreement between Burlington and Citibank

The largest funding source in question is the \$6 million to be financed through a special-situation lender. The city is engaging financial institutions to finalize terms for a lender to provide bridge financing secured by BT revenues and assets. The loan will give the city a period of time to sell BT and use the sale proceeds to finalize the settlement. The sale proceeds will need to repay the \$6 million bridge financing plus interest, provide additional net sale proceeds to cover the city's \$1.3 million payment and split remaining net sale proceeds equally with Citibank.

The settlement liability is more manageable than the risks associated with continuing the lawsuit. If the city does not obtain the special financing and a new partner to purchase the telecom, it could shoulder additional general obligation debt to cover the remaining \$7.3 million in financing sources. Assuming the city had to cover the difference by issuing debt, the amount would equal a 10% increase to its outstanding direct debt by dollar amount, and would increase the debt burden by 0.2 percentage points to almost 2% of the city's \$3.9 billion tax base.

The city cannot easily pay the settlement in full from operating revenues. Burlington's general fund has only recently stabilized from multiple years of operating deficits and the city has insufficient reserves available to immediately offset any financing gap. As of fiscal year ended June 30, 2012, the city's available fund balance was negative \$11.4 million (or negative 20% of revenues) attributed to the subsidies provided to BT. However, the city has increased its cash position and continues to control expenditure growth. We project the improved fiscal management will result in an operating surplus of \$300,000 in fiscal 2014, which the city could use to absorb additional debt service.

Burlington must also submit a petition for the Vermont Public Service Board (PSB) to approval the settlement by no later than 15 March. The PSB, in 2010 ruled that the city had to cease providing further subsidies to BT because it violated the city charter. We expect the PSB approval to focus on Burlington's ability to finalize the financing sources primarily from BT revenues and not from other city funds.

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