

Congratulations, you have been awarded a broadband stimulus grant! Now what?

Aim high and learn from
this success story how
your broadband
business can help local
economic development

ROBERT PICCHI AND TAD DERISO

THE AMERICAN RECOVERY AND REINVESTMENT ACT

(ARRA) established a resource pool of \$7.2 billion for the deployment of advanced communications networks in poorly served regions of the nation. With the community-contribution component and the leverage from the debt component, well over \$10 billion will be spent on broadband networks. Some grant recipients are established organizations with stable business processes. However, a number of organizations are nascent startups with no operational history, back-office support systems, or personnel. Looking back with the perfect clarity of hindsight, there are a number of valuable insights that can be shared from a similar project that pioneered the process of deploying communications networks for economic recovery.

VISION

Mid-Atlantic Broadband Cooperative, Inc. (MBC) aspires to **provide the leadership and technology infrastructure** necessary to assist in the economic revitalization efforts of southern Virginia. MBC will carry out its business in a way that is financially successful, i.e., independent of external funding sources. MBC will reinvest in the communities we serve and we will conduct ourselves and manage our business in a way that inspires confidence among our stakeholders.

MISSION

The mission of MBC is to **drive economic development** in the communities served, by providing wholesale telecommunications transport services. MBC will work aggressively to expand the reach of broadband services, offer new and enhanced services, lower the cost of doing business in the region, and promote innovation and reinvestment in the region.

Mid-Atlantic Broadband Cooperative (MBC) was organized, conceptually, almost 10 years ago to bring advanced communications services to southern Virginia, a region that was under served. The local economy was traditionally dependent on the manufacturing and agriculture sectors. These industries were in decline, with jobs disappearing and wages not keeping pace with the balance of the Commonwealth; worse yet, the decline would continue if intervention strategies were not implemented. A group of civic-minded business leaders, headed by the Future of the Piedmont Foundation and Old Dominion Electric Cooperative, crafted a plan to deploy advanced communications facilities to deliver wholesale, open-access, communications services. The ultimate objective—sow the seeds for future economic development.

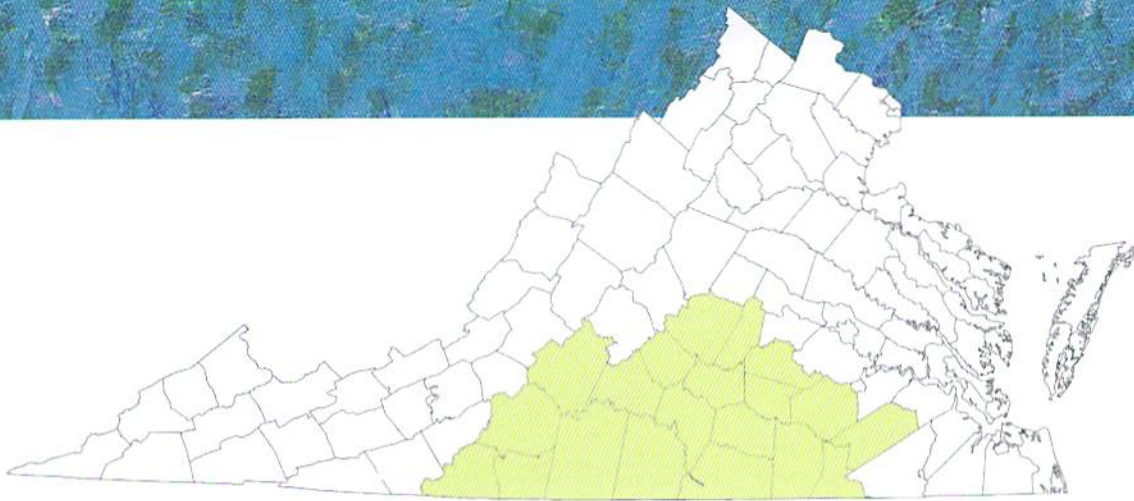
With the financial support of the Economic Development Administration (U.S. Department of Commerce), and the Virginia Tobacco Indemnification and Community Revitalization Commission, a 700-mile state-of-the-art network was developed and began providing services in 2006.

Today, MBC is a stable organization that is cash-flow positive and three years ahead of the original business plan projections in both top-line revenue and gross margin. The Virginia Economic Development Partnership calculates that MBC has created 2,188 jobs and nearly \$300 million in private-sector investment in southern Virginia. In December 2009, the Executive Office of the President published a report “Recovery Act Investments in Broadband: Leveraging Federal Dollars to Create Jobs and Connect America” citing MBC as a bright-shining example of “middle mile that works.”

While it is premature to declare absolute success—MBC prefers to measure success one day at a time—the company is clearly on a path to become a mature and stable business that is an engine of repurposing a region's economy.

Five Insights for Success

Looking back on its evolution, it is clear MBC has been fortunate, and enjoyed great mentorship from the providers of capital and a board of directors. But beyond good fortune and sponsors, MBC has also executed



well and done many things right that can provide a template—or at least a framework—for those who follow. There are five insights that every organization should be mindful of as they begin the process of planning their own success:

1. HIRE WELL. It is said the best thing you can do for your competition is hire poorly. While there may not be direct or apparent competition for many of the new communication startups because they are operating in un- and under-served markets, the lesson is still applicable. MBC began with no employees and through most of the planning and construction process relied on consultants and subject-matter experts. When the time came, the board of directors, and now management, took the hiring process seriously. Every hire is evaluated with great care and scrutiny. The company has been fortunate and has employed individuals who are self-reliant and each has made significant contributions. As MBC has grown, the skill-set requirements have changed, and we continue to add new and needed proficiencies as necessary. Hiring the wrong person can cost the organization two years—one year to recognize the mistake, and another to fairly dispatch and replace that resource.

In a *New Yorker* interview, John Doerr, a partner at Kleiner Perkins Caufield & Byers, the noted venture capital firm, once identified “managerial risk” as the single most important and difficult element to assess in any new business—far more difficult to evaluate than the technology, financial, and market risks. Get the right people and the organization will enjoy success. Also, consider that performance must be compensated. While many ARRA-funded telecom startups are not-for-profit, they are competing for the same resources as investor-owned companies.

The daunting challenges, obstacles, and hurdles of a startup argue for greater rewards; yet many not-for-profits balk at providing market-based compensation. Personnel cost will be the single greatest controllable element of cost of goods sold. As a startup strives to achieve cash-flow breakeven, there will be great pressure to do so by limiting labor costs. This is a mistake;



it is far better to take a slower path of providing market-based compensation, with a fair amount of at-risk compensation for performance, and take additional time to achieve breakeven.

MBC initial network build

2. MISSION STATEMENT. At some point early in the development of a business plan it is important to craft a vision and mission statement for the organization. Although this sounds obvious, many organizations do not work through this exercise believing their purpose is so obvious. In fact, it is critically important to define an enduring statement of purpose and values to guide an organization and its staff through decision-making processes. At MBC, every investment alternative, budgeting decision, and network-capacity issue is scrutinized in the clarity of the MBC mission statement. MBC’s purpose for existence is something every employee knows and understands. The mission is distilled to time-specific and measureable performance goals for the organization. Get the vision and mission statements right, and they will serve as a clarifying beacon for the successful development path of the new enterprise.

3. BREAKTHROUGH BUSINESS MODEL. An organization awarded a stimulus grant is presented an opportunity to do something truly exceptional—a breakthrough opening that shatters existing frameworks and challenges old business models. MBC poured considerable thought and analysis into developing that distinctive dimension to the business model. In MBC’s case it is pricing. Within the region, communications services had previously been priced as a function of



capacity and distance. Because of the newness of the network and the efficiency of an all-fiber network, we figured costs were largely fixed with very little variable costs for each new service, irrespective of distance. Accordingly, we developed a “postage stamp” pricing plan.

Much like letters delivered anywhere in the U.S. for the same price, MBC sells services anywhere on the 700 mile network for the same price. MBC prices as close to the marginal costs as possible, and there is no mileage sensitivity. Additionally, MBC has developed provisioning time as a focus for competitive advantage. New services have been turned up in as little as half a day. Pricing and in-service cycle times have dramatically changed the character of transport in the region. MBC’s efforts have been recognized as a major contribution in the relocation of several new technology-based businesses to the region, and for lowering the overall cost of doing business.

4. BOARD AND MANAGEMENT RELATIONS. By far the greatest source of problems for both boards of directors and management is the perception the other is overstepping its charter. The problem is not exclusive to telecommunications, startups, or non profits; it is universal. At the most dysfunctional level, managers want to craft policy, and boards want to make managerial decisions. MBC management and its Board enjoy very good relations—but, it had to be earned. This rapport has been a fount of opportunity for growth. In the early days of MBC’s development, the board met monthly and was actively involved in all decision-making. Management had no ability for discretionary spending, contract execution, or hiring.

Gradually, as the organization matured, and senior managers displayed solid judgment in their recommendations to the board, responsibility and authority were ceded to management. Today, the board meets quarterly and has carefully crafted planning processes to meet with management, establish policy, and exercise their powers to bring about desired results. The board measures management’s execution according to budgets and performance metrics established with management input. A successful mechanism employed by the MBC board to achieve this desired state was to

engage a board advisor who has been able to effectively work between the board and management as a liaison to achieve the evolved framework with few bruised egos. Maintaining high-quality board relations is an imperative for success. Any new enterprise has sufficient challenges dealing with customers, competitors, and regulators; do not let board relations become an additional challenge.

5. FINANCE AND ACCOUNTING. There are three important notions to consider in the area of finance and accounting. Each is sufficiently material to merit its own discussion, but they are somewhat linked.

► First is the notion that EBITDA is a meaningful metric to gauge a communications enterprise’s success. It is not. Yet industry insiders continually speak of EBITDA as the definitive gold standard. Earnings before interest, before taxes, and before depreciation and amortization is a partial measure of cash flow and a full measure of financial hijinks. Yet, somehow the industry has swallowed the tonic that achieving positive EBITDA is success. I believe the definition of EBITDA expressed by Berkshire Hathaway Vice Chairman Charlie Munger is the most accurate: *I think that, every time you see the word EBITDA, you should substitute the words “bullshit earnings.” To truly succeed, focus on NOPAT (net operating profit after taxes), and you will have no regrets.*

► Second is the thorny issue of dealing with depreciation and establishing reserves. Because the initial capital has been provided largely by external agencies, there will be a tendency to ignore depreciation expense. True, depreciation is a non-cash expense. Depreciation is a mechanism to account for the periodic consumption of the asset base. If you are not establishing a reserve of funds to replenish those assets, you are on a trajectory to consume all assets—a run-to-failure strategy.

As soon as practical, a startup must begin establishing a reserve for the replenishment of assets. It is impractical to think all depreciation expenses can be funded by a reserve fund at the outset. Set a goal of funding the short-lived assets first and gradually build upon those reserves until you are at least matching the total monthly depreciation expense. Achieving this




level of funding will be a long time coming, but it will instill an important discipline.

► Third, when selecting a financial software package aim high. In its nascent stage MBC's needs were simple—invoices were paid to vendors who were designing, permitting and building the network. Today, MBC is in a very different situation; a complex organization with multiple lines of businesses. To accommodate the business complexity, multiple migrations to more sophisticated software packages with greater functionality have been made. Each migration causes additional problems and loss of historical information. The communications business is fundamentally a high fixed-cost, asset-based, business; accordingly, there is a need for an asset management module that is not apparent in the early stages. Aim high in your initial accounting software selection, and it will save considerable disruption down the road.

Paying Forward Advice for Success

In retrospect, MBC has accomplished something truly noteworthy. While unsolicited advice is rarely welcomed, these observations are offered in homage to those who shared generously with MBC as we began our journey; particularly to Virginia Tech and its E-Corridors organization who provided the general business architecture for MBC.

Irrespective of the politics and one's personal thinking about the merits of stimulus spending, there is little disagreement that broadband services have a special character—that the common welfare of all people will be dependent on broadband. Applications such as healthcare, education, and e-government are completely reliant on broadband. This clearly places broadband service in the unique category of a utility service for all.

The best way to dispel criticism of stimulus-funded broadband programs is to perform well, accomplish what was agreed, conduct your businesses with vigilance, and comport yourselves with professionalism. 

*Robert Picchi is the president of the Blue Ridge Advisory Services Group, www.blueridge-group.com.
Tad Deriso is the president and CEO of Mid Atlantic Broadband Cooperative, www.mbc-va.com.*

Applications such as healthcare, education, and e-government are completely reliant on broadband. This clearly places broadband service in the unique category of a utility service for all.

