

MEMORANDUM

To: Scott VanDerMillen, City of Marshall, Minnesota
From: Brian T. Grogan and Erik L. Romsaas
Date: March 5, 2019
Re: FCC Form 394 – Clarity Telecom, LLC

INTRODUCTION

Clarity Telecom, LLC ("Clarity") submitted to the City FCC Form 394 ("Form 394") - Application for Franchise Authority Consent to Assignment or Transfer of Control of Cable Television Franchise ("Application"). Moss & Barnett has been retained by a number of jurisdictions, including the City, to review the Application.

Pursuant to Minnesota state law and the City's Franchise, this proposed change of control is prohibited without the written consent of the City. Federal law provides the City with a period of one hundred twenty (120) days to examine the legal, technical and financial qualifications of the proposed transferee – Python Intermediate II, LLC ("Python"). Under Federal law, if the one hundred twenty (120) days expires without action by the City, the Application is deemed granted. Given that Clarity will retain control of the Franchise as the "Grantee" following completion of the proposed transaction Moss & Barnett's review does not address the legal and technical qualifications of Clarity, but rather focuses solely on the financial qualifications as directed by the City.

FINANCIAL QUALIFICATIONS

Attached hereto please find Moss & Barnett's summary of the financial qualifications regarding Clarity's Application.

RESOLUTION REGARDING THE PROPOSED TRANSACTION

Also, attached hereto please find Moss & Barnett's proposed Resolution approving the transaction for the City's review and consideration.

If the City adopts the proposed Resolution, please forward one executed original of the Resolution to my attention at the address below. I will obtain the required signatures and return a fully executed document to the City.

~ END OF MEMO ~

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FINANCIAL QUALIFICATIONS

I. SCOPE OF REVIEW

PC III CTH Holdings, L.P., a Delaware limited partnership (“PC Holdco”), owns Clarity Telecom Holdings, LLC, a Delaware limited liability company, (“Clarity Holdings”) which is the 100% owner of Clarity Telecom, LLC, a Delaware limited liability company, (“Clarity”) the current holder of the cable television franchises (hereinafter referred to as the “Franchise Agreement”) granted by the Cities (collectively referred to herein as the “City”). Under the Franchise Agreement, Clarity operates cable television systems (the “System”) that provide cable services and other communication services in the City. PC Holdco has requested the City’s approval of the proposed pro forma transfer of control of Clarity Holdings and Clarity to Python Intermediate II, LLC, a Delaware limited liability company (“Python II”).

At the request of the City, Moss & Barnett, PA has reviewed selected financial information that was provided by Clarity or publicly available to assess the financial qualifications of Clarity.

The financial information that was provided or available through other public sources and to which our review has been limited, consists solely of the following financial information (hereinafter referred to collectively as the “Financial Statements”):

1. FCC Form 394 “Application for Franchise Authority Consent to Assignment or Transfer of Control of Cable Television Franchise” dated January 23, 2019, provided by PC Holdco (the “Application”), along with such other exhibits as provided therewith, with include the financial statements of Clarity; and
2. Such other information as is publicly available.

Our procedure is limited to providing a summary of our analysis of the Financial Statements in order to facilitate the City’s assessment of the financial capabilities of Python II to control and operate the System in the City. We have not requested any additional financial information from Python II or Clarity other than what was provided as part of the Application and what is available publicly.

II. OVERVIEW OF TRANSACTION

Through a series of mergers and other transactions pursuant to an Agreement and Plan of Merger dated as of December 24, 2018 (the “Transaction Agreement”) attached to the Application, Python II will own all of the equity interests of Clarity Holdings and, therefore, Clarity (the “Transaction”).¹ Clarity Holdings will continue to own Clarity, which will continue to provide service to existing subscribers.²

Clarity will continue to hold the Franchise with the City and continue to provide subscriber communication services pursuant to the current Franchise Agreement with the City, without interruption, or changes in rates, terms or conditions.³ Additionally, Clarity’s management team will not change as a result of the Transaction.⁴

¹ FCC Form 394 “Application for Franchise Authority Consent to Assignment or Transfer of Control of Cable Television Franchise” dated January 23, 2019, provided by PC III CTH Holdings, L.P. (the “Application”) at Exhibit I.I.2.

² Id.

³ Application at Exhibit IV.

⁴ Id.

III. OVERVIEW OF CLARITY

Clarity, doing business as Vast Broadband, is a broadband/cable company providing high-speed internet, cable television and digital telephone services for residential and business customers in South Dakota, northwestern Iowa and southwestern Minnesota.⁵

Cable providers and telecommunication companies operate in a competitive environment and the financial performance of cable television operators, like Clarity, are subject to many factors, including, but not limited to, the general business conditions, programing costs, incumbent operators, digital broadcast satellite service, technology advancements, burdensome service contracts, and customer preferences, as well as competition from multiple sources. The cable business is inherently capital intensive, requiring capital for the construction and maintenance of its communications systems. Each of these factors could have a significant financial impact on Clarity and its ability to continue to operate the System.

IV. FINDINGS

As part of our review, we have analyzed the Financial Statements, including the historical financial statements of Clarity.

1. **Analysis of Financial Statements.** Federal law and FCC regulations provide franchising authorities, such as the City, with limited guidance concerning the evaluation of the financial qualifications of an applicant for a cable franchise. In evaluating the financial capabilities of a cable operator, we believe it is appropriate to consider the performance of an applicant based on the applicant's historical performance plus its projected or budgeted financial information along with its financial capabilities (financing). We believe a general review of the historical Clarity financial information may provide some insight into its general financial operations, but we note that there are many unanswered questions regarding Clarity's operations going forward.

The Clarity financial information discussed below includes all of Clarity's operations. We have analyzed historical financial statements as of November 30, 2018, December 31, 2017 and 2016 in providing the information in this section.

2. Specific Financial Statement Data and Analysis.

(a) **Assets.** Clarity had (i) current assets of \$21.938 million, \$17.033 million and \$12.544 million and (ii) total assets of \$242.352 million, \$243.820 million, and \$270.903 million, as of November 30, 2018, December 31, 2017 and 2016 and November 30, 2018, respectively.⁶

(b) **Liabilities.** Clarity had (i) current liabilities of \$11.446 million, \$12.098 million and \$13.257 million; and (ii) long term debt of \$159.431 million, \$159.636 million, and \$185.815 million, as of November 30, 2018, December 31, 2017 and 2016, respectively.⁷

(c) **Income and Expense.** Clarity reported (i) revenue of \$77.335 million, \$84.579 million and \$83.189 million; (ii) operating expenses of \$67.764 million, \$73.362 million and \$72.256 million; and (iii) operating income of \$9.571 million, \$11.217 million and \$10.933 million for the year ending November 30, 2018, December 31, 2017 and 2016, respectively.⁸

⁵ <https://www.vastbroadband.com/about-vast/>.

⁶ Financial Statements at p. 4.

⁷ Id.

⁸ Financial Statements at p. 5.

Clarity posted net earnings of \$0.255 million and an overall net loss of \$1.827 million for the year ending December 31, 2017 and 2016.⁹

V. SUMMARY

Using the FCC Form 394 to establish an absolute minimum standard of financial qualifications that a proposed applicant must demonstrate in order to be qualified as the successor operator of the System, Clarity has the burden of demonstrating to the City's satisfaction that Clarity has "sufficient net liquid assets on hand or available from committed resources" to consummate the transaction and operate the System, together with its existing operations, for three (3) months. This minimum standard is not easy to apply to the complex organizational structure of Clarity and its owners, which include various entities and investment funds.

Based solely on Clarity's financial information that we reviewed and limited strictly to the financial information analyzed in conducting this review, we do not believe that Clarity's request for transfer of the System from one indirectly wholly-owned subsidiary to another indirectly wholly-owned subsidiary can reasonably be denied based solely on a lack of financial qualifications of Clarity.

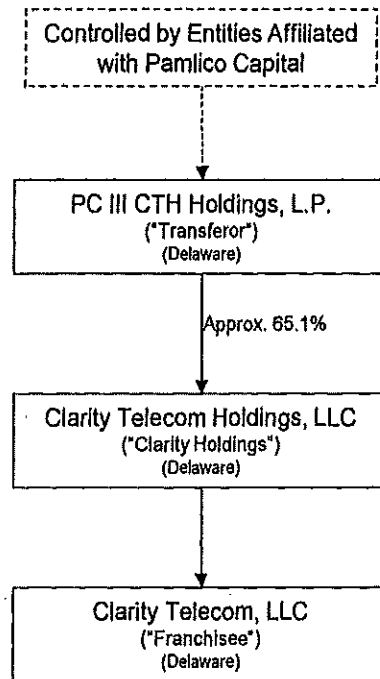
In the event the City elects to proceed with approving the proposed transfer of control, the assessment of Clarity's financial qualifications should not be construed in any way to constitute an opinion as to the financial capability or stability of Clarity to (i) operate under the Franchise Agreement, (ii) operate its other operations, or (iii) successfully consummate the transaction as contemplated in the Transaction Agreement. The sufficiency of the procedures used in making an assessment of Clarity's financial qualifications and its capability to remain the parent of the operator of the System is solely the responsibility of the City. Consequently, we make no representation regarding the sufficiency of the procedures used either for the purpose for which this analysis of financial capabilities and qualifications was requested or for any other purpose.

Lastly, in order to ensure compliance with its obligations to operate the System and since we have continued to base a significant part of our analysis on the Financial Statements of Clarity, we recommend that the City maintain any performance bonds or corporate parent guaranty required under any City Franchise Agreement.

⁹ Id.

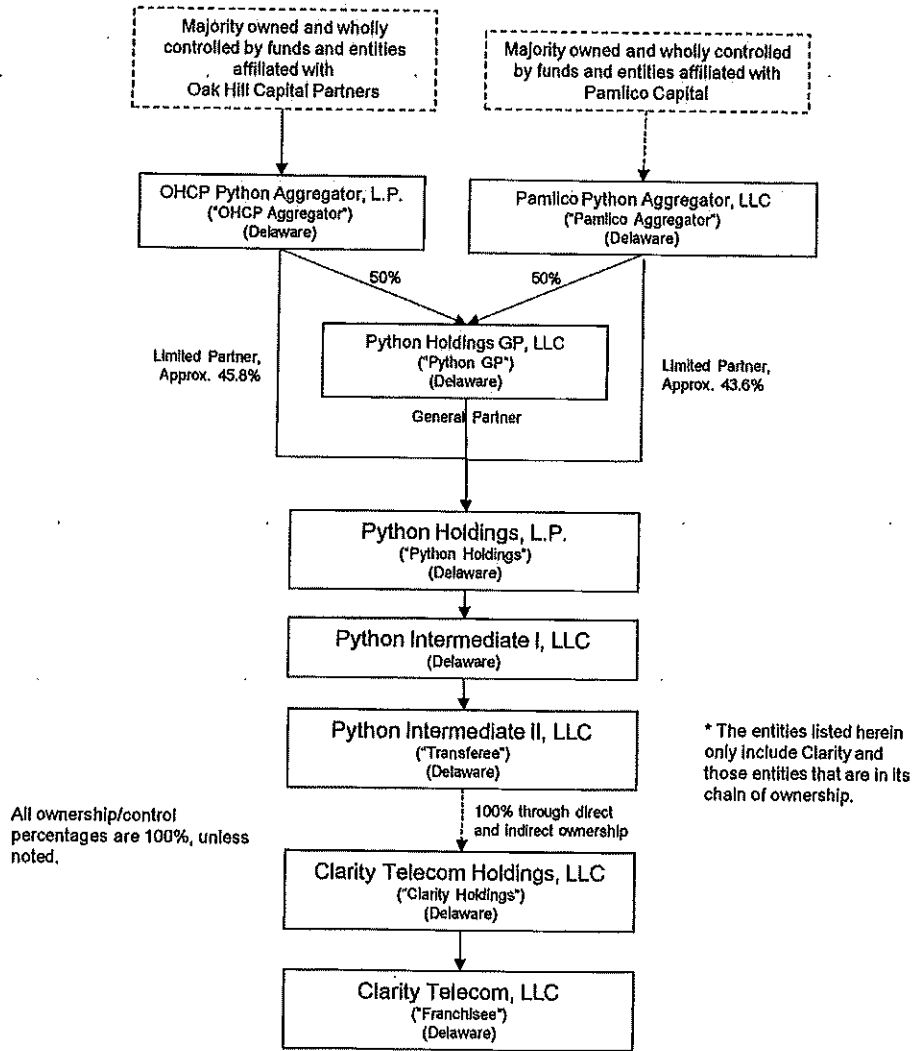
Current Control of Clarity*

* The entities listed herein only include Clarity and those entities that are in its chain of ownership.



All ownership/control percentages are 100%, unless noted.

Post-Transaction Control of Clarity*



RESOLUTION NO. _____

**APPROVING THE PROPOSED TRANSFER OF THE
CABLE FRANCHISE CURRENTLY HELD BY CLARITY TELECOM, LLC**

WHEREAS, Clarity Telecom, LLC, d/b/a Vast Broadband (collectively hereinafter referred to as “Grantee”), currently holds a cable television franchise (“Franchise”) granted by the City of Marshall, Minnesota (“City”).

WHEREAS, Grantee owns, operates and maintains a cable television system in the City (“System”) pursuant to the terms of the Franchise.

WHEREAS, the City received from Grantee, Federal Communications Commission Form 394 - Application for Franchise Authority Consent to Assignment or Transfer of Control of Cable Television Franchise, (“Application”) dated January 23, 2019.

WHEREAS, federal law and the terms of the Franchise require that the City take action to consider the Application within one hundred twenty (120) days of the date of receipt, or on or before May 23, 2019.

WHEREAS, Section 9.5(a) of the Franchise requires the City’s advance written consent prior to the Grantee’s transfer of the Franchise.

WHEREAS, the Application includes a copy of an Agreement and Plan of Merger, dated December 24, 2018, (“Agreement”) that provides for the acquisition of Grantee’s assets, including the Franchise.

WHEREAS, under the Agreement Python Intermediate II, LLC (“Python”) will acquire one hundred percent (100%) of the Grantee’s assets which include the Franchise (“Transaction”).

WHEREAS, as a result of the proposed Transaction Grantee and Python have requested consent from the City to the proposed transfer of the Franchise.

WHEREAS, the City has reviewed the proposed Transaction, and the legal, technical, and financial qualifications of the Grantee.

WHEREAS, based on information provided by Grantee and Python, and on the information received by the City, the City has elected to approve the proposed Transaction subject to certain conditions as set forth herein.

NOW, THEREFORE, the City of Marshall, Minnesota hereby resolves as follows:

1. All of the above recitals are hereby incorporated by reference as if fully set forth herein.
2. The Franchise is in full force and effect and Grantee is the lawful holder of the Franchise.
3. The City is not presently aware of any default by Grantee to comply with the terms, conditions, requirements, and obligations set forth in the Franchise, notwithstanding such, the City’s approval of the Transaction shall in no way be deemed a representation by the City that Grantee, or its successors in interest, are in compliance with the obligations under the Franchise. The City does not waive its rights with respect to Grantee's compliance with the terms,

conditions, requirements, and obligations set forth in the Franchise and other applicable law, including the City's right to compel Grantee, or its successors in interest, to comply with the provisions of the Franchise.

4. Grantee will remain the lawful holder of the Franchise after completion of the Transaction.

5. The City hereby consents and approves of the proposed Transaction subject to:

a. Closing of the Transaction described in information provided to the City by Grantee and Python in Federal Communications Commission Form 394 and related documents.

b. Grantee or Python shall, within thirty (30) days of the date of adoption of this Resolution, fully reimburse City for all of City's reasonable costs and expenses in connection with the City's review of the proposed Transaction, including without limitation, all costs incurred by the City for attorneys retained by City to assist in the review as well as any applicable notice and publication costs ("Reimbursement").

i. The Reimbursement shall not be deemed to be "Franchise Fees" within the meaning of Section 622 of the Cable Act (47 U.S.C. § 542), nor shall the Reimbursement be deemed to be (i) "payments in kind" or any involuntary payments chargeable against the Franchise Fees to be paid to the City by Grantee pursuant to the Franchise.

ii. The Reimbursement shall be considered a requirement or charge incidental to the awarding or enforcing of the Franchise.

6. In the event the proposed Transaction contemplated by the foregoing resolution is not completed, for any reason, the City's consent shall not be effective. If any of the conditions set forth herein are not met, the City's consent to the proposed Transaction shall be null and void and of no effect.

This Resolution shall take effect and continue and remain in effect from and after the date of its passage, approval, and adoption.

Approved by the City of Marshall, Minnesota this _____ day of _____, 2019.

ATTEST:

CITY OF MARSHALL, MINNESOTA

By: _____

By: _____

Its: _____

Its: _____

ACCEPTANCE AND AGREEMENT

Python Intermediate II, LLC and Clarity Telecom, LLC hereby accept this Resolution No. _____ (“Resolution”) and agree to be bound by the terms and conditions of this Resolution and the terms and conditions of the Franchise referenced within the Resolution.

Dated this _____ day of _____ 2019.

PYTHON INTERMEDIATE II, LLC

By: _____

Its: _____

Sworn to before me this _____ day
of _____, 2019.

NOTARY PUBLIC

Dated this _____ day of _____ 2019.

CLARITY TELECOM, LLC

By: _____

Its: _____

Sworn to before me this _____ day
of _____, 2019.

NOTARY PUBLIC