

**UTAH TELECOMMUNICATION OPEN
INFRASTRUCTURE AGENCY**

FINANCIAL STATEMENTS

JUNE 30, 2010

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
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**INDEPENDENT AUDITOR'S
REPORT**

Jensen & Keddington, P.C.

Certified Public Accountants

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Board of Directors
Utah Telecommunication Open Infrastructure Agency
West Valley City, Utah

We have audited the accompanying basic financial statements of Utah Telecommunication Open Infrastructure Agency (UTOPIA), as of and for the year ended June 30, 2010, as listed in the table of contents. These financial statements are the responsibility of UTOPIA's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of UTOPIA, as of June 30, 2010, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a separate report dated December 30, 2010 on our consideration of UTOPIA's internal control over financial reporting and on our tests of compliance with certain provisions of laws and regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Jensen & Keddington

December 30, 2010

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY MANAGEMENT DISCUSSION AND ANALYSIS

Introduction

The following is a discussion and analysis of the Utah Telecommunication Open Infrastructure Agency (UTOPIA) financial activities for the fiscal year ending June 30, 2010.

Description of Business

Fourteen Utah cities created UTOPIA, which constructs and operates a wholesale fiber telecommunications infrastructure, as a way to promote economic development and to improve the quality of life for their residents. The system is an open access network, which means UTOPIA constructs the network, which private providers use to offer retail digital services to customers in UTOPIA member cities. Two additional cities (Washington City and the town of Vineyard) joined UTOPIA in December 2007.

Eleven of the current UTOPIA member cities pledged sales tax revenues as partial loan guarantees in order to secure financing for the network. UTOPIA is currently in the process of constructing a wholesale advanced communications network within its Member cities. The Network is being built with fiber-to-the-premises technology, which transmits information at the speed of light, significantly faster than existing copper, cable, wireless or satellite systems. Fiber is currently used for the backbone of the Internet and other high-demand applications, but has not been widely implemented over “the last mile” into homes and businesses. UTOPIA is laying the fiber-optic cable necessary to connect each Member city and the homes and businesses within each city. UTOPIA’s fiber-optic cable is laid both underground and above ground, according to existing utilities infrastructure. Other elements of the Network include conduits, innerducts, fiber strands, splices, switches, transmitters, terminals, internal power sources and all other items necessary to operate the Network.

Highlights

As of the end of June, 2010, more than 1,700 miles of fiber cable (and associated duct) have been placed within the boundaries of the eleven members cities. Within the 73 production footprints there are a total of 62,000 addresses, of which 56,000 are able to receive services at the decision of the household or business (marketable). The remaining addresses are located in apartment buildings, condominium developments, or in areas isolated by right-of-way or pole access issues. Fourteen service providers—iWire, Brigham.net, Connected Lye, Fibernet, Fuzecore, Infowest, Integra Telecom, Nuvont, PAETEC, PrimeTime Communications, Telesphere, Veracty, Voonami, and XMission—were actively marketing at least some of their services and a total of 8,782 homes and businesses had subscribed to services by fiscal year end. These subscribers selected services as indicated in Figure 1. Since 2008, UTOPIA has been focusing on improving and growing network operations through a six-phase strategy:

- Refinance (June 2008)
- Create a baseline
- Operational Readiness
- Operation Prime
- Alternative Funding
- Full Deployment

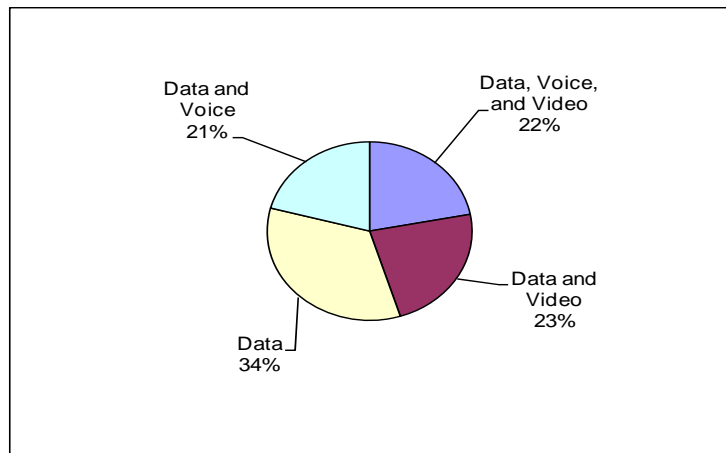


Figure 1

Chart showing breakdown of subscribers at June 30, 2010 by type of service selected.

Fourteen service providers—iWire, Brigham.net, Connected Lye, Fibernet, Fuzecore, Infowest, Integra Telecom, Nuvont, PAETEC, PrimeTime Communications, Telesphere, Veracty, Voonami, and XMission—were actively marketing at least some of their services and a total of 8,782 homes and businesses had subscribed to services by fiscal year end. These subscribers selected services as indicated in Figure 1. Since 2008, UTOPIA has been focusing on improving and growing network operations through a six-phase strategy:

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY MANAGEMENT DISCUSSION AND ANALYSIS (Continued)

The first three phases were completed rather quickly, and in October, 2008, Operation Prime was launched in Tremonton. Over the past couple of years, Operation Prime was completed using new fiber awareness techniques to improve awareness of the open service provider model and the benefits of a truly fiber-optic network. In particular, the UTOPIA model provides consumers with the power of choice, a key differentiator emphasized in messaging to UTOPIA markets. UTOPIA's fiber awareness efforts are highly targeted, ensuring the most effective tactics and messaging are used only in those areas that need it.

Operation Prime continued forward with rollouts in portions of Layton and West Valley and culminated in a complete city build-out in Brigham City. Over 30% of the residents signed up for the power of choice provided on the UTOPIA network, through a shared-build-cost model – each resident pays a portion of the total infrastructure cost to bring the fiber technology to their community. UTOPIA is now engaged in the final two phases of the strategy.

To help facilitate growth, the cities have formed another inter-local agreement, called UIA (The Utah Infrastructure Agency) as a separate entity to grow the UTOPIA network and provide more oversight on the growth of our community-owned fiber optic network in our cities. It also makes it easier for other cities that are interested in having this kind of network to join down the road.

Future growth of the network will follow a similar pattern to that of Brigham City; deployment will be largely demand-based, bringing the network first to those areas that will make the best utilization. Additionally, funding for future growth will be released incrementally, to ensure the most fiscally responsible use of money, reducing interest payments required over time and financial risk.

Overview of Financial Statements

The financial statements included in this report have been prepared in compliance with generally accepted accounting principles. The balance sheet provides information about the Agency's resources and obligations at year end. The statement of revenues, expenses, and changes in net assets presents the results of business activities during the course of the year. The statement of cash flows presents changes in cash and cash equivalents, resulting from operational and investing activities. Notes to the financial statements provide required disclosures and other information that are essential to the full understanding of material data provided in the statements. The notes present information about the Agency's accounting policies, significant account balances, obligations, commitments, contingencies and subsequent events.

As expected, the financial statements reflect conditions typical of a capital-intensive start-up enterprise in the first years of its existence. Operating revenue increased 19.2% over the prior fiscal year but did not cover operating expenses. UTOPIA's fiber awareness efforts continuously add new subscribers to the network and increase the Agency's gross revenues. It is anticipated that operating break even will be achieved in the upcoming fiscal year.

Operating revenues for the fiscal year fell short of budget (\$3,983,860 actual vs. \$5,218,400 budget. Operating expenses (expenses excluding interest and depreciation) were less than projected (\$5,958,238 actual vs. \$6,945,518 budget). Operating profit (EBITDA) was slightly less than projected. Depreciation and amortization expense were also below projected levels. Interest expense was \$15 million higher than anticipated, due to the swap mark to market valuation at the end of the year. Without the non-cash book adjustment of over \$16 million, interest expense for the year would have been \$1.2 million below budget.

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
MANAGEMENT DISCUSSION AND ANALYSIS (Continued)**

Table 1 - Summary of the Agency's Statement of Net Assets.

	2010	2009
Current and other assets	\$ 9,981,588	\$ 22,409,938
Capital assets	82,903,617	87,908,146
Total Assets	<u>92,885,205</u>	<u>110,318,084</u>
Long-term liabilities outstanding	257,334,927	234,505,561
Other Liabilities	1,971,347	2,244,514
Total Liabilities	<u>259,306,274</u>	<u>236,750,075</u>
Invested in net capital assets, Net of related debt	(28,255,400)	(21,835,947)
Unrestricted	<u>(138,165,669)</u>	<u>(104,596,044)</u>
Net Assets	<u>\$ (166,421,069)</u>	<u>\$ (126,431,991)</u>

Table 2 - Summary of the Agency's Statement of Revenues, Expenses and Changes in Fund Net Assets

	2010	2009
Revenues:		
Operating revenues	\$ 2,855,985	\$ 3,341,807
Interest income	69,400	539,236
Other revenues	191,644	-
Total Revenues	3,117,029	3,881,043
Expenditures:		
General and administrative	4,492,509	4,020,349
Network	1,465,729	1,511,202
Depreciation	6,419,454	6,038,132
Bond interest and fees	30,728,415	41,575,495
Other expenses	-	1,957,009
Total Expenditures	<u>43,106,107</u>	<u>55,102,187</u>
Change in net assets	(39,989,078)	(51,221,144)
Total net assets, beginning of year	(126,431,991)	(75,210,847)
Total net assets, end of year	<u>\$ (166,421,069)</u>	<u>\$ (126,431,991)</u>

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
MANAGEMENT DISCUSSION AND ANALYSIS (Continued)**

Capital Assets and Debt Administration

UTOPIA’s investment in capital assets, net of depreciation, was \$82.9 million at year end. Types of assets include outside plant (fiber and conduit), inside plant (electronics), customer premise equipment, construction in progress and other miscellaneous assets.

As of June 30, 2010, UTOPIA’s outstanding debt amounted to \$192.3 million. The majority of this debt (revenue bonds payable) is secured by the 11 pledging members’ sales tax pledges.

	<u>2010</u>	<u>2009</u>
Construction in progress	\$ 6,926,003	\$ 9,193,504
Outside plant	64,171,388	71,422,648
Inside plant	2,429,865	4,394,781
Customer premise equipment	7,592,473	838,907
Intangible right	1,378,661	1,448,441
Office furniture and equipment	297,665	430,688
Vehicles	107,562	179,177
	<u>\$ 82,903,617</u>	<u>\$ 87,908,146</u>

	<u>2009</u>	<u>2008</u>
Revenue bonds payable	\$ 185,000,000	\$ 185,000,000
Capital leases	484,115	623,598
Notes payable	6,849,903	135,750
	<u>\$ 192,334,018</u>	<u>\$ 185,759,348</u>

Final Comment

UTOPIA member cities launched the wholesale network project to facilitate economic development and to improve the quality of life for their residents. The telecommunication industry could replace its current copper wire and coaxial cable networks with a virtually unlimited-capacity fiber optic infrastructure, but business imperatives keep them from doing so. UTOPIA believes that the long-term return on such an investment would not meet investors’ short-term profit demands. As a municipality, on the other hand, UTOPIA believes that the long-term needs of their constituents are their first priority. UTOPIA expects that it can build and maintain the infrastructure that private companies have, thus far, been unwilling to do. This will provide the “pipe” through which private companies can provide the latest, most competitive services to consumers.

Since construction of the network has begun, there is evidence that these objectives are being served. Business location and expansion decisions have been influenced for the benefit of UTOPIA cities by the imminent availability of world-class connectivity. Competition for customers has prompted heavy marketing from incumbent providers and reductions in overall subscription rates for consumers. Market acceptance of the services that are available over the network is very positive.

BASIC FINANCIAL STATEMENTS

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
STATEMENT OF NET ASSETS
June 30, 2010

Assets

Current Assets:

Cash		\$ 284,622
Restricted investments		1,977,383
Receivables:		
Trade receivables, net	\$ 944,785	
Interest receivable - restricted investments	<u>690</u>	
Total Receivables		945,475
Inventory		2,166,166
Prepaid expenses		2,307,673
Notes receivable		15,783
Deferred charges		<u>76,005</u>
Total Current Assets		<u><u>7,773,107</u></u>

Noncurrent assets:

Capital Assets:

Construction in progress		6,926,003
Property and equipment, net		
Fiber optic network	75,572,387	
Office furniture and equipment	297,665	
Vehicles	<u>107,562</u>	
Total Property and Equipment, net		<u>75,977,614</u>
Total Capital Assets		<u><u>82,903,617</u></u>

Other Assets:

Deposits	10,686	
Deferred charges	<u>2,197,795</u>	
Total Other Assets		<u><u>2,208,481</u></u>
Total Assets		<u><u>\$ 92,885,205</u></u>

The accompanying notes are an integral part of these financial statements.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
STATEMENT OF NET ASSETS (Continued)
June 30, 2010

Liabilities

Current Liabilities:

Accounts payable	\$ 663,759
Accrued liabilities	115,519
Compensated absences	92,437
Interest payable	870,349
Capital leases payable	155,678
Deferred revenue	73,605

Total Current Liabilities	1,971,347
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Noncurrent Liabilities:

Compensated absences	94,431
Capital leases payable	328,437
Note payable	6,849,903
Revenue bonds payable	185,000,000
Swaps liability	65,062,156

Total Liabilities	259,306,274
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Net Assets:

Invested in capital assets, net of related debt	(28,255,400)
Unrestricted deficit	(138,165,669)

Total Net Assets	(166,421,069)
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Total Liabilities and Net Assets	\$ 92,885,205
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The accompanying notes are an integral part of these financial statements.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
For The Year Ended June 30, 2010

Operating Revenues	<u>\$ 2,855,985</u>
Operating Expenses:	
Payroll	2,290,769
Material and supplies	731,905
Professional services	1,469,835
Network	1,465,729
Depreciation	<u>6,419,454</u>
Total Operating Expenses	<u>12,377,692</u>
Operating Loss	<u>(9,521,707)</u>
Nonoperating Revenues (Expenses):	
Interest income	69,400
Miscellaneous income	191,644
Bond interest and fees	<u>(30,728,415)</u>
Total Nonoperating Revenues (Expenses)	<u>(30,467,371)</u>
Change In Net Assets	(39,989,078)
Total Net Assets, Beginning of Year	<u>(126,431,991)</u>
Total Net Assets, End of Year	<u><u>\$ (166,421,069)</u></u>

The accompanying notes are an integral part of these financial statements.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
STATEMENT OF CASH FLOWS
For The Year Ended June 30, 2010

Cash Flows From Operating Activities:	
Cash received from customers and users	\$ 4,225,966
Payments to suppliers	(3,247,184)
Payments to employees	<u>(2,278,536)</u>
Net cash used by operating activities	<u>(1,299,754)</u>
Cash Flows From Capital and Related Financing Activities:	
Purchase of property and equipment	(818,930)
Proceeds from sale of property and equipment	483,165
Proceeds from note payable	6,714,153
Bond interest and fees	(14,839,465)
Principal paid on capital leases payable	(139,483)
Restricted cash - net increase	<u>9,891,547</u>
Net cash provided from capital and related financing activities	<u>1,290,987</u>
Cash Flows From Investing Activities:	
Principal received on notes receivable	91,859
Interest income	<u>79,227</u>
Net cash provided by investing activities	<u>171,086</u>
Net Increase in Cash and Cash Equivalents	162,319
Cash and Cash Equivalents, Beginning of Year	<u>122,303</u>
Cash and Cash Equivalents, End of Year	<u><u>\$ 284,622</u></u>

The accompanying notes are an integral part of these financial statements.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
STATEMENT OF CASH FLOWS (Continued)
For The Year Ended June 30, 2010

Operating loss	\$ (9,521,707)
Adjustments to reconcile operating loss to net cash from operating activities:	
Depreciation expense	6,419,454
(Increase) decrease in current assets	
Accounts receivable	668,861
Inventory	433,418
Prepaid expense	(34,964)
Notes Receivable	627,514
Increase (decrease) in current liabilities	
Accounts payable	21,831
Accrued liabilities	12,233
Deferred Revenue	73,606
Net Cash Used by Operating Activities	\$ (1,299,754)

Supplemental Information

Noncash Investing, Capital, and Financing Activities:

Additions to outside plant includes \$60,914 of capitalized interest.

Interest expense of \$16,229,907 was added to the balance of swap liability.

Additions to capital assets includes inventory of \$1,018,246.

The accompanying notes are an integral part of these financial statements.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY NOTES TO FINANCIAL STATEMENTS

NOTE 1 SUMMARY OF ACCOUNTING POLICIES

Reporting Entity

Utah Telecommunication Open Infrastructure Agency (UTOPIA), a separate legal entity and political subdivision of the State of Utah, was formed on March 5, 2002, by an Interlocal Cooperative Agreement pursuant to the provisions of the Utah Interlocal Cooperation Act. UTOPIA's Interlocal Cooperative Agreement has a term of fifty years. During June 2004, the Board of Directors voted to amend the interlocal agreement with the member cities to allow pledging and non-pledging members. The pledging members were required to pledge sales tax revenue from their cities to partially guarantee payment of the bonds, and in return for the pledge, they would be the first to receive UTOPIA's services. The non-pledging cities did not pledge their sales tax revenue but their cities' network will be built when financing can be arranged that does not require a loan guarantee. There were 11 pledging members and 5 non-pledging members in UTOPIA at June 30, 2010. UTOPIA's purpose is to design, finance, build, operate, and maintain an open, wholesale, public telecommunication infrastructure that has the capacity to deliver high-speed connections to every home and business in the member communities.

Summary of Significant Accounting Policies

The accounting policies of UTOPIA conform to accounting principles generally accepted in the United States of America as applicable to government entities. UTOPIA applies all the pronouncements of the *Government Accounting Standards Board (GASB)*, and in accordance with GASB Statement No. 20, UTOPIA applies all *Financial Accounting Standards Board Statements and Interpretations* issued on or before November 30, 1989, except for those that conflict with or contradict GASB pronouncements. UTOPIA has the option to apply FASB pronouncements issued after that date and UTOPIA has chosen to do so.

The following is a summary of the more significant policies.

The Reporting Entity

In evaluating how to define UTOPIA for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in the related GASB pronouncement. The basic, but not the only, criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations and accountability of fiscal matters. The other criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether UTOPIA is able to exercise oversight responsibilities. UTOPIA does not have any component units, nor is it a component unit of any primary government.

Financial Statement Presentation and Basis of Accounting

UTOPIA prepares its financial statements on an enterprise fund basis, using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private businesses, where the intent is that all costs of providing certain goods and services to the general public be financed or recovered primarily through user charges, or where it has been deemed that periodic determination of net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (Continued)

Restricted Assets

UTOPIA maintains investments held by Wells Fargo for safekeeping of funds relating to service reserves and costs of issuance. When both restricted and unrestricted assets are available, it is UTOPIA's policy to use restricted assets first, then unrestricted assets as they are needed.

Property and Equipment

Property and equipment are stated at cost, which includes capitalization of interest costs incurred during construction. Normal maintenance and repair expenses that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements are capitalized and depreciated over the remaining useful lives of the related fixed asset. The net book value of property sold or otherwise disposed of is removed from the property and accumulated depreciation accounts and the resulting gain or loss is included as nonoperating revenues or expenses. Depreciation of property and equipment was computed using the straight-line method over the following estimated useful lives

Outside plant and certain customer premise equipment	25 years
Office furniture and equipment and vehicles	3-5 years
Intangible rights	25 years

Depreciation of inside plant and certain customer premise equipment was computed using an accelerated method over a 6 year life.

Retirement Plans

UTOPIA participates in three retirement plans. UTOPIA participates in a defined contribution plan, in the Utah Retirement System, and a union pension plan. Retirement plan costs are combined with employee benefits and are recorded on an accrual basis. It is UTOPIA's policy to fund the retirement plan costs as they are incurred.

Cash and Cash Equivalents

All non-restricted cash accounts are considered to be cash and cash equivalents for cash flow statement purposes.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is UTOPIA's best estimate of the amount of probable credit losses in the existing accounts receivable. UTOPIA has reserved \$500,362 of accounts receivable during the fiscal year. The revenue on these accounts has not been recognized and will be accounted for using the cost recovery method as described below.

Revenue Recognition

Revenue is generally recorded when the service has been provided, and profit is recognized at that time. In connection with certain sales, however, the related receivables are collected over extended periods of time and the collectability is uncertain. These sales are accounted for using the cost recovery method. Equal amounts of revenue and expense are recorded as these receivables are collected, and profit is only recognized after all costs have been recovered. Revenues are reported net of uncollectible amounts. Total uncollectible amounts related to revenues of the current period are \$1,127,875.

Inventories

Inventories are stated at the lower of cost or market using the first-in first-out method.

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)**

NOTE 1 SUMMARY OF ACCOUNTING POLICIES (Continued)

Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2 CASH AND INVESTMENTS

UTOPIA's deposit and investment policy is to follow the Utah Money Management Act. However, UTOPIA does not have a separate deposit or investment policy that addresses specific types of deposit and investment risks to which UTOPIA is exposed.

Utah State law requires that UTOPIA's funds be deposited with a "qualified depository" as defined by the Utah Money Management Act. "Qualified depository" includes any depository institution which has been certified by the Utah State Commissioner of Financial Institutions as having met the requirements as defined in Rule 11 of the Utah Money Management Act. Rule 11 establishes the formula for determining the amount of public funds which a qualified depository may hold in order to minimize risk of loss and defines capital requirements which an institution must maintain to be eligible to accept public funds.

The Utah Money Management Act also governs the scope of securities allowed as appropriate temporary investments for UTOPIA and conditions for making investment transactions. Investment transactions are to be conducted through qualified depositories or primary reporting dealers.

As of June 30, 2010, UTOPIA had the following deposits and investments:

<u>Deposit and investment type</u>	<u>Fair Value</u>
Cash on deposit	\$ 284,622
Investments in money market funds	1,977,383
	<u>\$ 2,262,005</u>

Cash on Deposit:

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, UTOPIA's deposits may not be returned to it. As of June 30, 2010, \$65,087 of the \$317,167 balance of deposits was exposed to custodial credit risk because it was uninsured and uncollateralized. UTOPIA has no policy to manage this type of risk.

Investment in Utah Public Treasurer's Investment Funds (UPTIF):

Interest rate risk. The risk that changes in the interest rate will have an adverse affect on the fair value of an investment. UTOPIA's investment UPTIF are not subject to interest rate risk.

Credit risk. This is the risk that an issuer or other counter party to an investment will not fulfill its obligations. As of June 30, 2010 the UPTIF in which UTOPIA has investments were unrated.

Concentration of credit risk. This is the risk of loss attributable to the magnitude of UTOPIA's investment in a single issuer. UTOPIA's investment in UPTIF is not subject to a concentration of credit risk.

Custodial credit risk – investments. This is the risk that, in the event of the failure of the counterparty to a transaction, UTOPIA will not be able to recover the value of its investments that are in the possession of an outside party. UTOPIA's investment in UPTIF has no custodial credit risk.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 3 RESTRICTED INVESTMENTS

Restricted investments consist of the following:

Debt service	\$ 1,977,383
Restricted investments - current	(1,977,383)
Noncurrent portion of restricted investments	\$ -

NOTE 4 PROPERTY AND EQUIPMENT

The following summarizes UTOPIA's property and equipment as of June 30, 2010:

	Beginning Balance	Additions	Deletions	Ending Balance
Capital assets, not being depreciated:				
Construction in progress	\$ 9,193,504	\$ -	\$ (2,267,501)	\$ 6,926,003
Total capital assets, not being depreciated	9,193,504	-	(2,267,501)	6,926,003
Capital assets, being depreciated:				
Outside plant	72,558,223	2,598,643	-	75,156,866
Inside plant	13,540,167	194,795	-	13,734,962
Customer premise equipment	11,588,263	846,729	-	12,434,992
Intangible right	1,624,040	-	-	1,624,040
Office furniture and equipment	838,621	42,259	-	880,880
Vehicles	401,274	-	-	401,274
Total capital assets, being depreciated	100,550,588	3,682,426	-	104,233,014
Less accumulated depreciation:				
Outside plant	(8,049,009)	(2,936,469)	-	(10,985,478)
Inside plant	(9,145,386)	(2,159,711)	-	(11,305,097)
Customer premise equipment	(3,831,078)	(1,011,441)	-	(4,842,519)
Intangible right	(180,443)	(64,936)	-	(245,379)
Office furniture and equipment	(407,933)	(175,282)	-	(583,215)
Vehicles	(222,097)	(71,615)	-	(293,712)
Total accumulated depreciation	(21,835,946)	(6,419,454)	-	(28,255,400)
Total capital asset, net of accumulated depreciation	78,714,642	(2,737,028)	-	75,977,614
Property and Equipment, net	\$ 87,908,146	\$ (2,737,028)	\$ (2,267,501)	\$ 82,903,617

Depreciation expense of \$6,419,454 was charged to operating expense for the year ended June 30, 2010. During the year, UTOPIA incurred interest expense of which \$60,914 was capitalized.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 5 LONG-TERM DEBT

The following is a summary of the changes in long-term debt obligations for the year ended June 30, 2010.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds					
2008 revenue bonds	\$ 185,000,000	\$ -	\$ -	\$ 185,000,000	\$ -
Total Revenue Bonds	185,000,000	-	-	185,000,000	-
Capital leases					
Equipment	316,840	-	(97,538)	219,302	105,402
Payson	161,415	-	(24,334)	137,081	25,311
Developer	145,343	-	(17,611)	127,732	24,965
Notes payable					
Pledging Members	-	6,714,153	-	6,714,153	
Non-pledging members	135,750	-	-	135,750	-
Compensated absences	120,243	66,625	-	186,868	92,437
Total Long-Term Debt	<u>\$ 185,879,591</u>	<u>\$ 6,780,778</u>	<u>\$ (139,483)</u>	<u>\$ 192,520,886</u>	<u>\$ 248,115</u>

Revenue Bonds

Taxable Adjustable Rate Advanced Communications Special Revenue and Refunding Bonds, Series 2008, original issue of \$185,000,000, principal payments due in quarterly installments beginning December 2013, interest payments due monthly at LIBOR, which was 2.83% at June 30, 2009, with the final payment due June 2040. The bonds were issued to finance UTOPIA's infrastructure construction and retire the Series 2007, 2006, and 2004 Revenue Bonds.

	<u>\$ 185,000,000</u>
Total Revenue Bonds	185,000,000
Less current portion	<u>-</u>
Noncurrent portion	<u>\$ 185,000,000</u>

UTOPIA is required by the Letter of Credit and Reimbursement Agreement (the Agreement) relating to the above Revenue Bonds to maintain a Debt Service Coverage Ratio (the ratio of net income to the maximum total annual debt service) of at least 1 to 1, measured at the end of each fiscal year. This financial covenant was not maintained at June 30, 2010. Management is currently in negotiations with the agent to receive forbearance on this ratio requirement, and management anticipates receiving the forbearance. However, if forbearance is not received, the Agreement states that agent and lender will not seek to secure the appointment of a receiver or receivers unless an event of default also occurs from the pledging members, as described in Note 9. A default from the pledging members is not anticipated; therefore the revenue bonds are reported as a noncurrent liability.

UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)

NOTE 5 LONG-TERM DEBT (Continued)

The following summarizes UTOPIA's revenue bonds debt service requirements as of June 30, 2010:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2011	\$ -	\$ 10,614,197	\$ 10,614,197
2012	-	10,614,197	10,614,197
2013	-	10,614,197	10,614,197
2014	5,000	10,614,030	10,619,030
2015	210,000	10,608,603	10,818,603
2016-2020	5,485,000	52,423,256	57,908,256
2021-2025	15,620,000	49,517,715	65,137,715
2026-2030	29,835,000	43,122,399	72,957,399
2031-2035	51,085,000	31,803,887	82,888,887
2036-2040	82,760,000	12,950,874	95,710,874
	<u>\$ 185,000,000</u>	<u>\$ 242,883,355</u>	<u>\$ 427,883,355</u>

Capital Leases

Capital leases consist of the following:

UTOPIA is obligated under a lease for the purchase of vehicles and equipment from a financing institution. Because the terms and options contained in the lease have effectively created a financing arrangement, UTOPIA is required to record this transaction as a capital lease. Lease payments are \$9,897 each including imputed interest at 7.78%. The capitalized cost of vehicles and equipment was \$661,783 with accumulated depreciation of \$471,190. \$ 219,302

UTOPIA is obligated to pay a developer for outside plant construction. Because the terms and options contained in the lease have effectively created a financing arrangement, UTOPIA is required to record this transaction as a capital lease. Lease payments are \$20 a month for each unit built in the subdivision. Interest is charged at 7.00% annual rate. The capitalized cost of outside plant construction was \$159,257 with accumulated depreciation of \$12,748. 127,732

UTOPIA is obligated under a lease for the use of a fiber optic network from Payson City. Because the terms and options contained in the lease have effectively created a financing arrangement, UTOPIA is required to record this transaction as a capital lease. Lease payments are \$30,792 each year including imputed interest at 4%. The capitalized cost of fiber optic network was \$259,739 with accumulated depreciation of \$37,233. 137,081

Less current portion (155,678)

Noncurrent portion \$ 328,437

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)**

NOTE 5 LONG-TERM DEBT (Continued)

Minimum lease payments for the years ending June 30 are as follows:

Equipment Lease			
2011	\$	182,670	
2012		182,670	
2013		63,912	
2014		63,912	
2015		47,672	
2016		-	
		<hr/>	
Total minimum lease payments		540,835	
Less amount representing interest		(56,720)	
		<hr/>	
Present value of net minimum lease payments	\$	484,115	
		<hr/> <hr/>	

Note Payable

The note payable consists of the following:

Amounts owed to pledging members. These amounts reflect the use of pledging members contributions to trustee for payments as required by Taxable Adjustable Rate Advanced Communications Special Revenue and Refunding Bonds, Series 2008. Interest is accrued at the current PTIF rate which was .59% at June 30, 2010. These debts are subordinate to the Taxable Adjustable Rate Advanced Communications Special Revenue and Refunding Bonds, Series 2008 and therefore will not be required to be paid back until that obligation is fulfilled.

\$ 6,714,153

Amounts owed to non-pledging members. These amounts will be paid when UTOPIA begins to build the network in the respective member's city. Management does not anticipate making any payments in the next fiscal year.

135,750

Total Note Payable 6,849,903

Less current portion

-

Noncurrent portion

\$ 6,849,903

NOTE 6 RETIREMENT PLANS

Plan Description

UTOPIA contributes to the Local Governmental Noncontributory Retirement System which is a cost sharing multiple-employer defined benefit pension plan administered by the Utah Retirement Systems (Systems). The Systems provide refunds, retirement benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries in accordance with retirement statutes.

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)**

NOTE 6 RETIREMENT PLANS (Continued)

The Systems are established and governed by the respective sections of Chapter 49 of the Utah Code Annotated 1953 as amended. The Utah Retirement Office Act in Chapter 49 provides for the administration of the Utah Retirement Systems and Plans under the direction of the Utah State Retirement Board (Board) whose members are appointed by the Governor. The Systems issue a publicly available financial report that includes financial statements and required supplementary information for the State and School Contributory Retirement System and State and School Noncontributory Retirement System. A copy of the report may be obtained by writing to the Utah Retirement Systems, 540 East 200 South, Salt Lake City, Utah 84102 or by calling 1-800-365-8772.

Funding Policy

Plan members are required to contribute a percent of their covered salary (all or part may be paid by the employer) to the respective systems to which they belong. UTOPIA is required to contribute 11.66% of the covered salary to the Noncontributory System. The contribution rates are the actuarially determined rates. The contribution requirements of the Systems are authorized by statute and specified by the Board.

UTOPIA's contribution to the Noncontributory System for the years ending June 30, 2010, 2009, and 2008 were \$165,365, \$147,985, and \$35,267, respectively. The contributions were equal to the required contributions for each year.

UTOPIA is legally obligated to contribute to the retirement systems as long as they have employees meeting membership requirements.

UTOPIA contributes to a non-contributory defined contribution retirement benefit plan covering substantially all employees. Currently all of the assets and income of the 457 Plan are held in trust by the plan administrator for the exclusive benefit of the participants or their beneficiaries rather than as assets of UTOPIA. Employer contributions under this plan during the years ended June 30, 2010, 2009, and 2008, were \$22,420, \$97,613, and \$23,484, respectively.

UTOPIA contributes to a union pension plan. Contributions are based upon hours worked by employees covered under an agreement and are funded on a current basis. Employer contributions to the plan during the year ended June 30, 2010, 2009, and 2008 was \$109,395, \$163,324, and \$248,937, respectively.

NOTE 7 OPERATING LEASE

UTOPIA has entered into various operating leases to secure network operations facilities, office space and equipment. The current year's expense related to operating leases was \$545,558. These leases range from 3 years to 20 years. Total remaining minimum lease payments at June 30, 2010 are as follows:

2011	\$	459,126
2012		371,388
2013		340,194
2014		347,314
2015		162,202
2016-2020		586,010
2021-2025		61,010
2026		3,051
		3,051
	\$	2,330,295

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)**

NOTE 8 COMMITMENTS AND CONTRACTS

In conjunction with the 2008 Special Revenue and Refunding Bonds issued, UTOPIA was required to obtain a letter of credit. UTOPIA pays an annual fee for this letter of credit, which is 1.25% of the outstanding principal of the 2008 Special Revenue and Refunding Bonds. The unused letter of credit is \$186,773,973 at June 30, 2010.

NOTE 9 PLEDGING MEMBERS LIABILITY

The 11 Pledging Member's of UTOPIA have pledged sales and use tax revenues to partially guarantee payment of UTOPIA's Revenue bonds. In return for the pledge, these members will be among the first cities to receive UTOPIA's services. In June of 2008, UTOPIA issued an \$185,000,000 revenue bond. The first two years of bond payments will be made from a debt service reserve fund, funded by the debt. From that point on, until the bonds are due in June 2040, net revenues from UTOPIA will reimburse the debt service reserve fund for payments on the bond debt. To the extent that there are insufficient net revenues to pay the debt service, 10 Pledging Members are required to reimburse the UTOPIA debt service reserve fund of any shortfall by their respective percentages of ownership up to a specific dollar amount and one Pledging Member is required to reimburse the UTOPIA debt service reserve fund a specific amount. The Pledging Member's percentage of the debt service reserve shortfall is listed below, with a corresponding annual maximum liability. Any amounts paid by Pledging Members to UTOPIA to reimburse the debt service reserve fund will be a loan to be repaid by UTOPIA.

At June 30, 2010, the Pledging Member's had on deposit with the UTOPIA 2008 Debt Service Reserve Account the amounts specified below. These funds will remain on deposit until the bonds are retired. The debt service fund is required to increase June 1st of each year by 1.8275% compounded annually until it reaches approximately \$20,300,000.

<u>Pledging Member</u>	<u>Share of Total Pledge</u>	<u>Amount on Deposit</u>	<u>Maximum Pledge *</u>
Brigham City	3.33%	\$ 122,169	\$ 405,238
Centerville City	3.32%	121,504	403,028
Layton City	16.61%	609,823	2,022,787
Lindon City	3.06%	112,251	372,336
Midvale City	6.03%	221,220	733,786
Murray City	12.23%	449,117	1,489,725
Orem City	21.70%	796,278	2,641,258
Payson City	2.58%	94,519	259,920
Perry City	0.82%	29,970	99,409
Tremonton City	2.51%	92,175	305,745
West Valley City	27.82%	1,020,755	3,385,850
	<u>100.00%</u>	<u>\$ 3,669,781</u>	<u>\$ 12,119,082</u>

* These amounts are the fiscal year 2010 maximum debt service that can be required of the Pledging Members.

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
NOTES TO FINANCIAL STATEMENTS (Continued)**

NOTE 10 DERIVATIVE ARRANGEMENTS

UTOPIA has two derivative contracts that attempt to fix the interest rate so that an interest rate payment is known.

The terms, fair values, and credit ratings of counterparties for the various swap agreements at June 30, 2010 are summarized in the following table:

Interest Rate Swaps

Outstanding Notional Amount	Fixed Rate Paid by UTOPIA	Variable Rate ¹ Received by Counterparty	Fair Value	Swap Termination Date	Counterparty Credit Rating		
					S&P	Moody's	Fitch
\$ 110,000,000	5.787%	LIBOR-.046%	\$ (39,574,980)	July 1, 2040	A+	Aa3	A+
75,000,000	5.665%	LIBOR-.044%	(25,487,176)	July 1, 2040	A-	A2	A-

¹ Three month U.S. Dollar London Interbank Offered Rate.

The notional amounts of the swaps match the principal amounts of the associated debt. The swap agreements contain scheduled reduction in notional amounts that follow scheduled amortization of the associated debt.

NOTE 11 SUBSEQUENT EVENTS

On August 18, 2010, Utopia received notice that it was awarded \$16,229,321.00 in Federal stimulus grants under the Recovery Act. This grant was formally accepted on September 8, 2010 by Utopia agreeing to comply with all the award provisions.

**UTAH TELECOMMUNICATION OPEN
INFRASTRUCTURE AGENCY**

SUPPLEMENTARY REPORTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2010

**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
SUPPLEMENTARY REPORTS
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Jensen & Keddington, P.C.

Certified Public Accountants

Jeffery B. Jensen, CPA

Gary K. Keddington, CPA

Brent E. Christensen, CPA

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**INDEPENDENT AUDITORS' REPORT
ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Directors
Utah Telecommunication Open Infrastructure Agency
West Valley City, Utah

We have audited the financial statements of Utah Telecommunication Open Infrastructure Agency (UTOPIA), as of and for the year ended June 30, 2010, and have issued our report thereon dated December 30, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered UTOPIA's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of UTOPIA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of UTOPIA's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether UTOPIA's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which is described in the accompanying *Schedule of Findings and Recommendations*.

This report is intended for the information and use of the Board of Directors and management of UTOPIA and the Utah State Auditor's Office and is not intended to be and should not be used by anyone other than these specified parties.

Jensen & Keddington

December 30, 2010



Jensen & Keddington, P.C.

Certified Public Accountants

Jeffery B. Jensen, CPA

Gary K. Keddington, CPA

Brent E. Christensen, CPA

Jeffrey B. Hill, CPA

Gregory B. White, CPA

**INDEPENDENT AUDITOR'S REPORT
ON STATE OF UTAH
LEGAL COMPLIANCE**

Board of Directors
Utah Telecommunication Open Infrastructure Agency
West Valley City, Utah

We have audited the financial statements of Utah Telecommunication Open Infrastructure Agency (UTOPIA), for the year ended June 30, 2010 and have issued our report thereon dated December 30, 2010. As part of our audit, we have audited UTOPIA's compliance with the following general compliance requirements identified in the *State of Utah Legal Compliance Audit Guide*:

- Public Debt
- Cash Management
- Purchasing Requirements
- Other General Compliance Issues
- Utah Retirement System Compliance
- Fund Balance Limitation

UTOPIA did not receive any major grants during the year ended June 30, 2010.

The management of UTOPIA is responsible for UTOPIA's compliance with all compliance requirements identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about UTOPIA's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed an immaterial instance of noncompliance with the requirements referred to above, which is described in the *Schedule of Finding and Recommendation*. We considered this instance on noncompliance in forming our opinion, which is expressed in the following paragraph.

In our opinion, UTOPIA complied, in all material respects, with the general compliance requirements identified above and the requirements governing types of services allowed or unallowed; eligibility; matching, level of effort, or earmarking; reporting; and special tests and provisions that are applicable to each of its major State assistance programs for the year ended June 30, 2010.

This report is intended for the information and use of the Board of Directors and management of UTOPIA and the Utah State Auditor's Office and is not intended to be and should not be used by anyone other than these specified parties.

December 30, 2010

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**UTAH TELECOMMUNICATION OPEN INFRASTRUCTURE AGENCY
SCHEDULE OF FINDING & RECOMMENDATION
For the Fiscal Year Ended June 30, 2010**

State of Utah Legal Compliance

Finding

UTOPIA had deficit net assets in the amount of \$166,421,068. The Utah State Code 10-6-117 requires UTOPIA to maintain positive net assets.

Recommendation

We recommend that UTOPIA work to reverse this net asset deficit and comply with Utah State Code 10-6-117 on positive net assets.



RESPONSE TO SCHEDULE OF FINDING & RECOMMENDATION For the Fiscal Year Ended June 30, 2010

State of Utah Legal Compliance

Finding

UTOPIA had deficit net assets in the amount of \$166,421,068. The Utah State Code 10-6-117 requires UTOPIA to maintain positive net assets.

Recommendation

We recommend that UTOPIA work to reverse this net asset deficit and comply with Utah State Code 10-6-117 on positive net assets.

Response

UTOPIA does have a net asset deficit as stated above. The financial statements reflect conditions typical of a capital-intensive start-up enterprise in the first years of its existence. Operating revenue did increase 19.2% (without write-offs) over the prior fiscal year and steps are being taken to reverse the deficit. Some of those efforts are described below.

Since 2008, UTOPIA has been focusing on improving and growing network operations through a six-phase strategy:

- Refinance (June 2008)
- Create a baseline
- Operational Readiness
- Operation Prime
- Alternative Funding
- Full Deployment

The first three phases were completed rather quickly, and in October, 2008, Operation Prime was launched in Tremonton. Over the past couple of years, Operation Prime was completed using new fiber awareness techniques to improve awareness of the open service provider model and the benefits of a truly fiber-optic network. In particular, the UTOPIA model provides consumers with the power of choice, a key differentiator emphasized in messaging to UTOPIA markets. UTOPIA's fiber awareness efforts are highly targeted, ensuring the most effective tactics and messaging are used only in those areas that need it.

Operation Prime continued forward with rollouts in portions of Layton and West Valley and culminated in a complete city build-out in Brigham City. Over 30% of the residents signed up for the power of choice provided on the UTOPIA network, through a shared-build-cost model – each resident pays a portion of the total infrastructure cost to bring the fiber technology to their community. UTOPIA is now engaged in the final two phases of the strategy.

In addition, UTOPIA continues to add service providers to the network, which will also help reverse the deficit.