

## *INTRODUCTION & SUMMARY*

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This report has been precipitated by an opportunity, not by a problem. Our water system is in good shape and all quality metrics meet or exceed NJ State mandates. However, we have been presented with the opportunity to sell the MKL water system to a public Water Utility. The Association Board chartered a Water Committee to study the opportunity, to evaluate a proposal from Aqua New Jersey to buy the system, and to make a sell/hold recommendation to the board. The committee has performed due diligence; has informed, solicited feedback and addressed further questions from residents. It is the recommendation of a majority of the committee members that the Board should proceed with a recommendation to the community to vote authorization to sell the system. Furthermore, the committee recommends that the net sale proceeds be used by the Lakeshore Company to help in the payment of its debt, passing the benefit through to residents in the form of lower Association dues.

The rationale for the Committee's Sale Recommendation can be summarized as follows:

- 1. Sale will reduce MKLA's expenses and investment requirements. \$573 per-year, per member will be freed up** and can to be returned to members in the form of a dues reduction<sup>1</sup> without any change to our projected bank balances, cash flow, planned projects or ability to cope with unplanned projects in other community assets. Residents will receive a monthly bill from Aqua NJ, but they will gain control of water usage driven costs. Having meters (either in the basement or

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<sup>1</sup> The Committee recognizes that the board and community might wish to use some of the amount of \$573 made available to fund other capital expenditures or to preclude the need for future dues increases caused by inflation in other operating expenses. That decision is of course up to the Board and Community, but it does not impact this analysis. It just represents an alternative use of the funds made available by a sale of the water system.

underground) means that some residents will pay less than \$573 annually and some may pay more.

2. **Sale will provide the community with a water system run by a professional water company.** By professional we mean a company that makes its living by constructing, and operating water systems, uses documented Standard Operating Procedures, and is staffed with trained engineers who have extensive experience in running, repairing and improving water systems. In contrast, MKL's water company has been run by volunteers. For decades, a series of extraordinarily dedicated and hardworking volunteer Vice Presidents/Water System Managers with varying degrees of technical knowledge have taught themselves the ins and outs of our system. Additionally, the Association hires Agra Environmental to test our water and to provide technical advice. We noted, however, that at MKL all decisions about the system are in the hands of the volunteer Water System Managers, we do not have formal training courses and we do not have documented Standard Operating Procedures. In short, current operations are not conducted with the same rigor seen in a public, for profit Water Company. While the committee was very impressed with the amount of time our volunteer Water System Managers have invested in gaining a unique expertise about our system, it questioned whether in the future we would be able to consistently find volunteers with the time and commitment to gain such in-depth knowledge.
3. The water system is approximately 85 years old. It will continue to take substantial investment to keep it operating and we have been surprised by costly repairs in the past. Reserves are established for future maintenance, but not to replace the main pipes, the tanks, or for expenditures required by future regulatory requirements. The main pipes (90% of the system) do appear to be in good shape (we inspect them whenever we have to repair minor leaks). **Sale removes the need for all water system reserves and the risk that we may under reserve.**
4. **There are potential liabilities associated with providing water.** Due diligence has convinced us that there is no material

- risk of chemical pollution of our aquifer<sup>2</sup> and we believe the chances of someone seeking damages from the community for any reason are very small. However, we do not carry liability insurance for illnesses caused by our water and it would be costly to defend any lawsuit for the community and volunteers.
5. Commercial water companies earn their profits through investment in infrastructure spread across their entire NJ rate base. Aqua NJ's rate base includes 56,000 households. Selling the system is comparable to placing our water system in a large insurance pool rather than being self-insured. Because it receives a statutory return on any new capital investment that is deemed reasonable by the State, **Aqua NJ is incited to maintain and improve our system.**
  6. **Outages such as have occurred with JCP&L are not relevant to our water system** because our pipes are underground and, like our PSE&G gas lines, are not vulnerable to surface storms. Aqua NJ had no adverse service impact during Hurricane Sandy, gave good service to its customers, and is committed to installing a generator to maintain power to the pumps (either one of which can run the system) through future storms. .

This report opens with a more detailed discussion of the committee's recommendations and the rationale for the positions taken, both on sale and on use of sale proceeds. The balance of the report captures the salient background, issues, and findings of the committee.

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<sup>2</sup> See Appendix I