

Water System Project Information Session

December 12, 2012

These notes contain questions, comments, and suggestions made during the Dec. 12, 2012 Inform Meeting. Items beginning with a "Q:" are questions, and are followed by lines beginning with "A:" which are answers. Most "Comments" are followed by "Responses". Answers to questions, or responses to comments, except where noted by names in parentheses, are from the Water Committee.

These items incorporate the items registered on the easel by Don Kuhn.

Some Questions don't yet have answers. The Water Committee is researching these. This document will be updated when the research is completed.

This document was last updated on December 18, 2012.

- 1) Q: Who were the other Commercial Water Companies (CWCs) contacted?
A: White Water Utilities Inc., NJ American Water Co., United Water.

- 2) Q: If the CWC bills Lakeshore (community meter) would they bill at a commercial rate?
A: No. This question is only applicable in the case of a community-wide meter. The billing would be at a residential rate. Although the billing would go thru Lakeshore, Lakeshore would not be buying the water. It would just be a pass-thru agent for billing.

- 3) Q: Is either bidding company facing more of a burden from Sandy damage?
A: unknown. The committee will investigate.

- 4) Q: How many households are in the NJ water system?
A: unknown - The committee will investigate.

- 5) Q: Has the committee looked at leasing vs. selling the assets? Leasing would give us option to move to different provider.
A: We have not looked at leasing.

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6) Q: Will the CWC be able to sell water pumped at MKL outside of our community?

A: Slide 20 of the presentation discusses this. In short one bidder has said this is not economically viable. Several regulatory and legal hurdles would stand in their way. Harding Township prevented NJ American from running water pipes under township roads. Dave Dietz mentioned that Harding might make interconnection with other distribution systems difficult, as it is not interested in having water pipes extended throughout the township.

7) Q: Were the tariffs current?

A: Yes, they are 2012 tariffs. They are now posted on the MKL website.

8) Q: What is basis for water use?

A: We assume 250/gals per day per residence.

9) Q: What is included in the improvements proposed by the CWCs? Are the generator and the chlorine analyzer in the cost?

A: Both bids include about \$100K for the same type of improvements. About \$40K of the \$100K is for meters (if meters are installed). The remaining \$60K includes gas generators, and chlorine analyzers. See slide 11.

10) Q: Is the amount Lakeshore plans to spend in its capital plan for the water system more or less than the CWC will spend?

A: It is a bit difficult to compare. MKLA's capital plan estimates spending of \$182K between 2013 and 2019. This includes \$82K for Alpine main replacement in 2018. The current MKLA plan is given on slide 28 (a backup slide not shown at the Inform meeting). The CWCs said they will initially spend \$100K (of which \$40K is for meters) for upgrades. However they will also repair and replace any piping that gives them trouble. So they would replace the Alpine mains if necessary, and do many of the other repairs indicated in the MKLA plan.

11) Q: What has been the history of rate increases by the CWCs?

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A. Between 5.5% and 6.5% per year. See slide 13 for an historical cost analysis.

12) Comment: The rates the CWCs would charge look attractive considering that MKLA has large gaps in its insurance (e.g. product liability).

Response: The MKLA costs will certainly rise, perhaps dramatically, if we remedy the perceived gaps in insurance.

13) Q: If the tanks are destroyed is there insurance coverage?

A: We are insured for the damage to the tanks, but we are not insured for the cost of delivering water while the tanks are repaired/replaced.

14) Q: Would we have to wait to put in the generator if the closing will take 1-2 years in the future?

A: If we buy a generator before the purchase is completed, the buyer will reimburse us for its cost. (As a condition of this, they would want input into the selection of the generator).

15) Q: Do we know how much water we lose through leakage?

A: The average for water companies such as ours is about 10%. Later in the meeting, Ken Heiden asserted that about 1/3 of the water pumped was lost to leakage. Committee will investigate. See item # 58.

16) Q: Would the CWC perform a leakage evaluation prior to taking over the system?

A: The CWC would perform a leakage test **after** taking over the system.

17) Q: Has either bidder considered the cost of replacing the water tanks and mains?

A: The bidders have performed on-site inspections of our system. They know what they are buying. The costs of replacing any aged infrastructure will, in effect, be borne by all (approx. 60,000) of their NJ customers. They will be reimbursed for their (legitimate) expenses at MKL.

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18) Q: Did either of the bidders ask about 2 inches steel pipes?

A: They all are aware of the 2 inch steel pipes.

19) Q: Are the bidders aware of the state of well #3?

A: Yes.

20) Q: Is there a risk of either company going bankrupt?

A: Both companies have been around more than 100 years, and are in solid financial positions. Having said that, mismanagement could always produce a bankruptcy. In this case they would be liquidated, and their assets would probably be bought by another water company. In no case would MKL be left without a functioning water supply.

21) Q: If they go bankrupt would the community have a say in the transfer?

A: Very likely not. This would proceed through a bankruptcy court.

22) Q: Would the CWC be required to include more additives than a self-maintained system?

A: No. The only additive required of a purchaser is chlorine. All water companies are held to the same standards in chlorine treatment of water.

23) Q: How does the size of our system compare to the company's portfolio of customers?

A: Most of their customers are larger than us, but they have as customers some communities roughly the size of MKL.

24) Q: Slide10 indicates that Middlesex has only 60,000 of its 450,000 customers in NJ. Yet you say it is primarily a NJ company. How can that be?

A: Most of the other customers are indirect – Middlesex sells wholesale water to other water companies.

25) Q: Do either company have operation centers near us?

A. The committee will follow up.

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- 26) What will be the response time for the CWC to get on-site in the case of an emergency?
A: Assuming the roads are not blocked, we would estimate that someone would arrive within ½ hour.
- 27) Q: Chlorine is very corrosive to machinery. How frequently would the monitoring of our system be conducted by the CWC?
A: Automated monitoring equipment would be installed to give daily chlorine readings. In person visits would occur approximately weekly.
- 28) Q: Was Southeast Morris County Municipal Utilities Authority Board (SMCMUA) contacted for interest in our system?
A: Committee will investigate.
- 29) Comment: The risk to the MKL of its water system running dry is not listed on slide 19. The CWC would be responsible to bring the community water.
Response: We have added that to the second row on slide 19.
- 30) Comment: DEP regulations change over time. There is no proactive planning at MKL on regulatory requirements. The committee should add this risk to slide 19.
Response: We have added that to slide 19.
- 31) Comment: AWWA and NJ water source provide information of water regulation.
- 32) Q: What is the condition of our aquifer? Past validation of water during droughts showed we had plenty.
A: (Chris Allyn paraphrased) Our source of water is through fractured rock. It is not one big pool of water. Pump #1 is an artesian well, and running pump #2 will reduce the artesian flow in well #1. (Jim Irving) During droughts the wells have had no drop in “draw down”.

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- 33) Q: Would the customer base from the CWC be exposed to impacts of fracking?
A: committee will follow up.
- 34) Q: Did Aqua answer the question about selling MKL well water outside of MKL?
A: No.
- 35) Q: Would Harding need to approve the piping and sale of water to other customers?
A: Yes.
- 36) Q: What are the min & max levels that the CWC would be allowed to chlorinate our water? Would the increase in chlorine be used to offset some insurance risks?
A: CWCs are held to the same standards as MKL. The committee will provide actual technical specs on required chlorine levels.
- 37) Comment: The CWC might be incented to replace our mains due to the age of the pipes, but it is unlikely given the good condition of our 4 inch mains. Later comment: Law requires 6" mains so the CWC could use that as a basis for increasing investment.
Response: The cost of main replacement would be borne by all 60,000 of the CWCs customers. Other than the dislocation of such construction, MKL would get a good deal.
- 38) Q: Do we have access to company client references?
A: Yes. The committee will be checking references.
- 39) Q: Who would pay for the meters?
A: The CWC.
- 40) Comment: The pay back to start paying more than we are now for water would be over 7 years based on price difference.

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Response: If the net proceeds of the sale were fully distributed to the community, it would have the effect of offsetting water charges for a number of years. Depending on the amount distributed and what taxes were owed on this distribution, it is reasonable to estimate that the price difference between what a CWC charges and what is paid in dues to upkeep the water system would be zero for five+ years.

41) Q: If community-wide (aggregate) metering were in effect, would leakage be built into the price?

A: Yes, the CWC would build in such leakage. Extraordinary spikes in usage would be investigated by the CWC. Other leakage, e.g. someone leaving a hose on, would be borne by the community if metering is community-wide. Metering at the houses removes considerations of paying for leakage in the system.

42) Q: Would the investment include adding non-existent curb-stops?

A: If meters were installed, non-existent curb stops would also be added.

43) Q: How do the rates increase over time?

A: Slide 13 shows the history of rate increases. The average increase is about 5-6%/yr. The increases come every 2-3 years.

44) Q: Were there any requests by the CWCs to be able to access the lake water as a source?

A: (Dave Molendyke) No, lake water is not suitable for residential consumption.

45) Q: How did we pay for the repairs required for past large piping repairs?

A: The question is directed at the large MKL water expense spike in 2007. Because of bureaucracy at the state level, our payments for lake dredging were delayed. This delay allowed us to have sufficient cash on hand to pay for the spike in 2007 water system costs.

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46) Q: Are there any notes from previous discussions by the MKL Boards with water companies?

A(Chris Allyn): Check in the history room.

47) Q: If we go with a CWC will we face a higher Compound Annual Growth Rate (CAGR) in rates than the cost of self-maintaining the system?

A: It appears that the current MKLA CAGR for water expenses is about 1% - 2% lower than the CWCs' CAGR (this equates to \$6 - \$12 less per year). However, the costs of running the water operations to MKL may rise substantially if some of the uninsured risks (e.g. Product Liability) became insured. Insurance costs would then dominate MKL expenses in running the water company. The fluctuation in insurance costs may then change the CAGR for MKL. Also, large capital expenses for repairs can significantly increase MKLA's average cost increases.

48) Q: How far do we need to get into negotiation to see the CWC's contract terms?

A: We assume the CWCs have a generic contract and we will ask for it, if it is available. At this point both the committee and the CWCs are reluctant to do contact work until there is apparent willingness on the part of the community to sell. This may be a chicken-or-egg problem: Some residents may condition their vote on a contract, but we don't proceed to contract until we know that there is a sentiment to sell. Since we can't have 95 people negotiating the contract, we will need to defer the actual negotiations to the committee and the Lakeshore lawyer, with the MKLA and Lakeshore Boards approving the contract. What the committee needs to know is what terms/conditions are "show stoppers" for the community.

49) Q: How much due diligence have CWCs done on MKL's water system.

A: They have done on-site inspections of our water plant and have gotten historical records on operations (e.g. amount of water pumped, age of equipment, etc).

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- 50) Q: Would the CWC need to perform additional due diligence when we decided to move forward?
A: If we decide to move forward the companies would need to perform some additional due diligence procedures in advance of the contracting process.
- 51) Q: Have the bidders talked to Agra? (note: Agra is a firm under contract to MKL to be its licensed operator for the MKL water system).
A: The committee has talked to Agra. Agra also has a relationship with the bidders, and possibly could be a sub-contractor to them in the event of a sale.
- 52) Q: What is Agra's viewpoint on the potential sale?
A: Agra has been helpful in helping the WC analyze the situation. Agra's position on sell/hold is neutral.
- 53) Q: Is there any benefit from a real estate perspective to have a CWC run the water system?
A: This question was directed to the real-estate professionals in the room. No answer was recorded.
- 54) Q: Has it been easy or difficult to get volunteers to support the water system?
A: The VSA is currently staffed. There was some discussion on whether or not in the future we would have the engineering-oriented skills necessary to support the water system. A suggestion was made to consider promoting to new residents an interest in maintenance and familiarity with the existing system.
- 55) Q: What is the financial impact on me if we sell?
A: If you are an **average consumer** and we have meters you will see an increase in cost of water of about \$100/yr. (if you use relatively little you could see a drop in your costs). If there are no meters it will be about even. These figures do not take into account:

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- the benefit of the sale proceeds.
- the potential increase in MKLA dues if uninsured risk becomes insured.

56) Q: What are the tax implications on sale of assets?

A: We need to investigate the amount, if any, of the capital gains tax on a sale.

57) Q: Has the need for additional insurance to protect the community in the event of an impact to our water supply been discussed with the board?

A: As it has not yet received the WC's report, the board has not discussed the risks mentioned on slide 16 or the need for insurance.

58) Comment (Ken Heiden): During the power outage the water usage was not significantly reduced, so there must be considerable leakage in the system. If we use residence meters, residents don't assume the cost of any leakage in the system (other than leaks in their own property). The average cost of metered water might be less than the \$600 the committee is using for CWC pricing. Ken believes there might be as much as 1/3 leakage of the amount pumped. Residence level metering would thus reduce the average metered bill by \$200/yr (from \$600/yr to \$400/yr.)
Response: We agree that the more leakage there is in the current system the lower the average bill will be if individually metered. However, our usage is believed to be about average for communities with our demographics. The WC will review volumes during the hurricane.

59) Q: When conducting due diligence can you see if there have been any restrictions placed on other water systems after their takeover?

A: The committee will follow up on this.

60) Q: What are the service level agreements in place to return service in case of outage?

A: The committee will follow up.

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- 61) Q: Might there be benefit in interconnecting with a local water company to provide back up?
A: It would seem so. If our water source were jeopardized we could get water from another source. Evidently there are lines nearby. The committee has not had discussions with that company. Dave Dietz mentioned that Harding might make such an interconnection difficult, as it is not interested in having water pipes extended throughout the township.
- 62) Suggestion – Put on website the follow up points that will be included in the due diligence.
A: The follow-up points (from the easel sheet) are included in this document, which is posted on the MKL website.
- 63) Q: Would the CWC increase water pressure so the hydrants can be used to fight fires?
A: The fire department seems to prefer pumping lake water to fight fires at MKL.
- 64) Q: When was the last time the rate of return was changed for the CWC?
A: both companies received rate increases in 2012, and seem to get them every 2 years or so. We are not sure when the actual rate of return itself was changed. We will find out.
- 65) What restrictions on water use could the CWC impose on the community?
A: The main restrictions on use come from government authorities during drought. It is not in the CWCs economic interest to restrict water use.
- 66) Comment: Thanks to the Committee for its commendable work.