



Alaimo Group

200 High Street, Mt. Holly, New Jersey 08060 Tel: 609-267-8310 Fax: 609-267-7452
2 Market Street, Paterson, New Jersey 07501 Tel: 973-523-6200 Fax: 973-523-1765

September 14, 2015

G. Bruce Ward, Esq., Executive Director
Atlantic City Municipal Utilities Authority
401 North Virginia Avenue
Atlantic City, NJ 08401

Re: Atlantic City Municipal Utilities Authority
"Ernst and Young Draft Analysis of
Potential Savings"
Our File No. A-1130-0013-000

Dear Bruce:

Our office and the accounting firm of Bowman & Company LLP have reviewed the Ernst and Young draft Report related to the operation of the ACMUA water system integrated into the City's Public Works Department. Their Report recommendation is to modify the rate schedule to achieve a \$3,500,000 increase in revenue and decrease expenses by \$5,758,051 to achieve a net revenue to the City of \$9,258,051.

Their revenue theory is that the ACMUA "average" City rates are "approximately 40% lower on average" than "other water utilities in the County." The present water usage "overage" rate is approximately \$3.75 per 1000 gallons. This rate generally applies to all residential as well as nonresidential users. As a bulk user the average rate for NJAWC was \$3.4043 per 1000 gallons for the first nine (9) months in 2015. The ACMUA has increased rates in the past four years a total of approximately sixteen (16%).

In 2014, the revenue derived from Residential users was approximately \$4,700,000±, and the revenue from Nonresidential (business and commercial) was \$8,100,000. New Jersey American Water Company NJAWC, a reseller of water to neighboring communities, paid approximately \$1,900,000. The revenue summary is as follows:

	<u>Income</u>	<u>Percent</u>
Residential	\$4,700,000	32%±
Nonresidential	\$8,100,000	55%±
NJAWC	<u>\$1,900,000</u>	<u>13%</u>
Total	\$14,700,000	100%

- Consulting Engineers -

Civil • Structural • Mechanical • Electrical • Environmental • Planners

In order to achieve an added revenue target of \$3,500,000 from the Nonresidential users and NJAWC, their rates would have to be increased by more than 35%. The large water users are NJAWC and the Casinos. A 35% increase does not seem practical in a one year period. The decline in Casinos will reflect a decrease in ACMUA annual revenue, so that the 35% would be more like 50%-60% in the next five years based on future annual increases for inflation and lost revenue. There is a possibility that NJAWC would reduce or stop their purchase quantity if the rates are increased drastically.

The Report deals with the Administration Expenses first. They are proposing a reduction of \$2,219,443 from a 2015 Budget of \$3,041,366 for a reduction of 73%±. Part of the reduction is \$690,857 which is presently paid to the City as a hosting fee. Therefore, the "net saving" to the City would be \$1,528,586. This net saving is redefined later in the Report.

The bulk of the Administration "savings" are based on a 58% (\$618,972) reduction in Personnel Expenses; with a "combination of retirements and staff reduction." Their Report "attachment" seems to indicate out of a staff of fourteen (14), the Executive Director and the Staff Engineer would be terminated along with two (2) other workers. Three (3) people would be "retired" or "terminated." It is difficult to believe that a \$15,000,000 a year business would not need a top leader. Regulatory State and Federal reporting and business leadership is not a shared service.

Their proposed "savings" benefit costs are "reduced proportionally" to staff reduction. The largest savings is defined as \$383,330 from Health Benefits. This is a questionable number, since a portion of the Budget should include at least present retirees (estimated at \$150,000±). Going forward forced "retirements" of three (3) people will cost approximately \$23,000 each annually added to the existing retiree's costs. The reduction to Operating Expenses of \$273,000 as part of Administration Costs are severely flawed. To represent "savings" for postage, office supplies, printing, janitorial supplies, other, telephone, and electric is simply wrong.

The Report proposes the abandonment of the building on Virginia Avenue. The building does not just house Administrative staff but the major user of the complex is the Plant Operations staff and vehicles, equipment and materials which prior to 1980, were in the main plant in Pleasantville. The relocation has saved annually thousands of dollars in travel time and extended equipment life. An "abandoned" building does not stop costing the Owner money. The Insurance and other costs would increase. Subletting the building is a questionable answer in a declining market for office space. The maintenance facilities should be maintained for better access to their distribution systems and customers. It is difficult to believe the City can provide equal space at no added cost to themselves.

Their Repair and Maintenance saving of \$24,000 is again simply a wrong assumption.

The Miscellaneous Expenses savings of \$803,357 contains the \$690,857 that the ACMUA contributes to the City. The other items are for the most part building and vehicle costs which are not related to this "savings" for the fewer number of employees. This "savings" is a wrong assumption.

The oversimplifications that staff duties can be absorbed by City employees at no cost are not logical answers.

The next area of "savings" are proposed in Plant Operations staff reductions. The ACMUA water treatment plant is required by the State DEP, to have two (2) plant operators on duty 24 hours/day for 7 days/week. The system includes a complex water treatment plant, booster pumps, and a distribution system approximately 150 miles long and 1400 fire hydrants for fire protection. There are three (3) storage tanks with a combined capacity of nine (9) million gallons, two (2) surface reservoirs with a capacity of 500 million gallons, sixteen (16) deep wells, and one (1) Aquifer Storage Recharge (ASR) well. The water discharged from the Pleasantville Treatment Plant is discharged via two (2) 48" cast iron water mains mounted above ground on cradles supported by timber piles across tidal marshes to Atlantic City. The Missouri Avenue Main is 4.8 miles long and has been in service since 1916. The Albany Avenue Main is 4.4 miles long and has been in service since 1936.

Most of the water system was constructed prior to 1972. Some of it dates back to the early 1900's. In 2014 there were approximately 8,127 customer services ranging from 1" to 12" in diameter. The water system is "Iconic" in age and character with a mixture of surface water and well water. The system has a firm capacity of 24.52 MGD. The system's size and age requires full time attention to avoid costly and dangerous water outages.

The Report's major "savings" in Personnel expenses for Plant and System Operation are for staff reductions of \$1,952,741 or 52.63% of the Budget of \$3,710,256. They propose twelve (12) forced retirements and twenty (20) terminations out of the present staff of sixty-one (61); leaving twenty-nine (29) employees to operate and maintain the system. That would be a dangerously risky situation. Curiously they have decreased salary overtime costs by \$100,000. If they reduce staff by 50% ± they will more than double the overtime costs.

They reduce costs for Employee Benefits by \$1,363,198 for staff reduction numbers. The present cost for retirees Health Benefits which are estimated at \$422,000 ± per year are not defined. Neither are the forced "retirements" cost for twelve (12) people at \$23,000 each/year.

Office supplies costs are reduced by \$8,300, as a cost passed on to the City. This would not be a savings to the City.

Plant Expenses are reduced for chemicals by \$25,000 with no explanation. Gasoline costs are reduced by \$35,000 because of "fewer vehicles and employees." The distribution system will still require site visits for maintenance regardless of the number of employees.

Outside Service Expenses are reduced by \$275,000 for General Insurance for the "Elimination of office building and combination with City insurance." This statement does not stand the light of day. The building is part of the Operation capability. The balance of the insurance costs are related to the water system. The City insurance costs will be impacted if they assume ownership. The proposed savings of \$125,000 from the "Reduction in security needs" is a terrible assumption.

Both the Training, Travel and Education costs and the Dues and Subscription costs are "Reduced by 50%" due to fewer employees. In most cases, these are Organization (Authority) expenses and operator license renewals costs required by the State. Under Repairs and Maintenance Expenses a reduction of \$276,000 is proposed by transferring the costs to the City. This would not be a savings to the City. There are another \$85,000 costs being shifted to the City for Buildings and Grounds and Machinery. Again this would not be a savings to the City. The balance of the saving, \$45,000, is related to the reduction in staff, again which is grossly overestimated.

It is very difficult to critique a Report that is working backward from a conclusion. It is not possible to decrease the Budget by \$6,000,000 ±. The water rates should not be increased in one year by \$3,500,000; it would be a bad business decision.

The Authority supplies the basic water needs to the Community. It is also affected by the depressed economy. For the first six (6) months of 2015, the water usage was off by 17% for the same period in 2014. Fortunately the rate increase of 7% at the start of 2015 should balance the reduced loss from Casino closings in 2014.

The worst thing that can happen is to avoid the maintenance of the water system so that it falls back to 1980 condition of disrepair and water outages. There is no mention of capital expenditures for equipment upgrades and replacements.

The Report does not present an accurate analysis of their potential cost "savings."
They are greatly overstated.

Very truly yours,

ALAIMO GROUP



Richard A. Alaimo, P.E., P.P.
President

RAA/glm

c: Mr. Kirk Applegate, CPA, RMA, Partner, Bowman & Company LLP