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To: Shawn LaTourette, Acting Commissioner, NJ Department of Environmental Protection
From: David Zimmer, Executive Director, NJ Infrastructure Bank
Cc: Patricia Gardner, Assistant Commissioner, NJ Department of Environmental Protection
Date: January 19, 2021
Re: WIPA Emergent Condition Review for the Salem City Drinking and Clean Water Systems

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Charge – Determine whether Salem City, with respect to its Drinking Water and Clean Water treatment systems has demonstrated that it lacks the financial capacity to adequately address any of the four Emergent Conditions pertaining to the WIPA Act or cannot own and operate its system in a way that supports economic on a sustainable basis.

Financial Metrics

1. Cash on Hand / Liquid Reserves:
   a. **$0.3M** net cash (decreasing in recent years)
   b. **32 days** of Operating Expenses (very low number)
2. Current net income:
   a. **$0.46M** (Excludes debt service; Includes $0.3M from Gen'l Budget and Operating Surplus)
3. Coverage Ratio:
   a. **0.55X** (i.e. not enough cash to cover current debt payments w/out additional cash support from the General Fund)
4. 5-year Increased Debt Service based on Systems' CIP needs:
   a. **$0.97M** - based on 3% interest rate calculations provided in R&V Report. Coverage Ratio drops to 0.25X
5. Debt Ratio = Debt / Assets): looks at
   a. **84%** (Typical range is 60-70%. Limits systems' ability to borrow for new capital projects)
6. Water Charges as [%] of Median Household Income (n.b. rates below are calculated based on Salem City's MHI of $24,841, not the County's. As the systems serve the City, these are the accurate – and more challenging numbers):
   a. **5.59%** Current (unacceptably high)
   b. **8.73%** Pro-Forma (includes increased rate for new debt for emergent capital needs. Well above range)
7. Current Rating(s):
   a. **Moody's Ba3** (02/12/2020 Report included)

The financial metrics provided by the City of Salem (City) for their Drinking Water and Clean Water systems clearly show the systems are operating at negative cash flow and net income and, as such, are a drain on the City's General Fund. Historic underinvestment has resulted in substantial capital needs ($14.46 million over the next five years pursuant to the R&V Report) with limited capacity to leverage further. The low MHI of the system's rate base limits the ability to increase rates to offset the cost of investment. Any projects that produce budget-positive cash flow should be prioritized, a potential example being AMI internet-based water meters which increase revenue through the capture of more accurate usage/cost while lowering the expense of obtaining such data. In sum, the above metrics highlight the precarious position of the Salem City's Drinking Water and Clean Water systems.

Conclusion – It is the opinion of the New Jersey Infrastructure Bank that Salem City lacks the financial capacity to adequately address the needs of its water systems and operate them on a sustainable basis. As such, pursuant to its submission and based on the information provided in such submission, Salem City satisfies the requirements of the WIPA Act Emergent Condition #5.