

To: Edgewood Town Council and Mayor

From: Raymond H. Seagers

FACTS ON FEASIBILITY OF THE TOWN OF EDGEWOOD PURCHASING THE EPCOR WATER SYSTEM

I have reviewed the Preliminary Engineering Report prepared by Wilson & Company which has attempted to build a case for Edgewood to purchase the Epcor Edgewood and Thunder Mountain water system which currently serves a portion of the Town of Edgewood but also has many customers in Torrance County and Santa Fe County.

The report starts out suggesting the system be purchased for \$12,000,000 plus \$2,500,000 for town startup of a water department and other estimated fees, all with borrowed taxpayer's money. The \$14,500,000 would purchase the system and make several immediate short term improvements such as a) a new connection of a 12" line under Interstate 40 which is estimated to cost \$350,000, and b) adding water softening to the system, an improvement which is later totally eliminated as a possibility because of the tremendous cost to set up and operate those types of systems. This cost is not covered in the \$14,500,000 total cost of purchase.

The first question that comes to mind is whether or not the \$14,500,000 (all borrowed by the town) is a good investment of the people's money? A review of the projections of gross income and expenses and debt payments are set up in the exhibits and tables at the end of the PER. The optimistic projection (Table 6.1) purports to show that the town can pay all of its operating and administrative expenses plus loan payments and net \$377,258 per year. These numbers are based on operating and administrative expenses of \$793,200 to run the system and 2705 customers paying \$2,143,025 in annual revenue. The problem is the annual expenses reported by Epcor for the combined Edgewood and Thunder Mountain systems, in their required last report to the Public Regulation Commission was \$1,140,202 for operating and maintenance (found in an Appendix to the PER.) This real world figure of \$1,140,202 for operations and maintenance wipes out almost all of the estimated net return for the town (leaves \$8,256.00). Would any prudent investors to include the people of Edgewood, invest \$14,500,000 to receive a return on their investment of \$8,256.00 or .006% return on their investment? Would they even under the most optimistic pro forma suggested in the PER, invest \$14,500,000 to receive \$377,258 or 2.6%? This is a bad deal!

It gets worse when you consider the extra items of expense that are not addressed in the budget calculations which have been paid by Epcor over the years regarding inferior size water line replacement. The combined systems have a total of 237,053 linear feet of substandard water mains (40%) that do not meet appropriate residential or commercial fire flow requirements demanded by the Town of Edgewood. Epcor has been replacing these lines from time to time as the need arises to extend a water main or just to improve the system (Table 2.5). These new lines need to be 6" or 8" or larger. A real time cost for such replacements is \$50 to \$55 per linear foot or 237,050' X \$50 or \$11,852,650. If only half of this figure (\$5,926,325) is replaced over the next five years (\$5,926,325/5), it would be

\$1,185,265 each year added to operating expense, or if replaced over 10 years it is \$592,632 annually. Which of these liability figures do you believe is correct and do you think it is wise to ignore it when obligating the town to a \$14,500,000 debt?

The trend for many small towns that own their own systems is to sell out to companies like Epcor because there is no truth to the myth that a small town can achieve “economy of scale” by adding whole departments of people (6 new employees in this PER scenario paid at just under the poverty level) and then run efficiently. Epcor has 20+ people from engineers on down to equipment operators who can respond to any emergency in their New Mexico operations either in Edgewood, Albuquerque or the Clovis area, and has a very efficient billing operation in Phoenix which demonstrates real “economy of scale.”

You do not have to look far to see the terrible results small towns and other political units get into taking over a water utility. Eldorado at Santa Fe formed a water and sewer district and took over their original developer’s water system. They ended up in multiple lawsuits and were forced to pay quite a bit more for the system than they ever imagined. Their affordable tap on fee was at \$400.00 prior to taking on the system and now exceeds \$14,000.00. They have eliminated most residential growth and any affordable housing and are close to default. This result can be verified by the primary local landowner Joe Miller, who has been developing portions of his ranch in El Dorado for the past 40 years.

There are dozens of examples of this type of tragedy and sophisticated case studies done to analyze this very problem.

The argument that dealing with the PRC, the elected commission and multilevel professional department in Santa Fe that controls rate increases for utilities is a “problem,” is a real myth. This body has accountants, lawyers and other professional disciplines on staff who review very complicated rate increase applications on behalf of the public and are far more protective of rate payers’ interests than our local, very unsophisticated officials who are currently considering rate increases to our citizens with no oversight and no critical analysis to justify such increases. The PRC is the rate payers’ best advocate, but will not be consulted if the town makes costly mistakes and looks to its utility users to raise cash.

It is important to realize that the PER mentions community engagement and that several meetings were held to inform the public that Edgewood was considering this condemnation of the water system. I attended two of those meetings which drew quite a few residents and other concerned parties. The sentiment of the majority of each crowd was more than 80% against the town taking over the water system. There was discussion of the desire of many to explore softening the water but no one was in favor of significant increases in their rates to accomplish this improvement. Most participants were Epcor customers both in and outside of town limits. Little or no communication effort was given to attract Edgewood citizens who were on wells or other water systems. They were not informed that they also would be on the hook for the \$14,500,000 loan to the town of Edgewood which, in the event of default by the town, could greatly affect their property values and property tax liability.

The portion of the PER that serves as a sales job and rates from 1 to 5 the pros and cons of town ownership of the water system is completely flawed or naïve and falsely points to the advantage of full town government control of all future development. It praises the fact that town officials will determine who can develop their property and who shall be denied some property rights by 5 elected officials. This is not an advantage! All of our finest developments had no problem dealing with Epcor and in fact the advantages of dealing with this regulated entity supplies more flexibility for financing and fair treatment than any government owned utility can match.

When the government selects a certain area or portion of town that it will only serve with water then a false scarcity of developable land occurs and prices skyrocket, and almost no development occurs. The privately owned utility can reward that landowner who extends water across the lands of others thereby increasing their land value by negotiating a “grant in aid of construction” to the owner extending a main which can be structured to repay the developer over a period of time a portion of his money expended for the excess line extension as others tap on to the main. Towns do not often do this though they reap the benefit of all new tap-ons. This is the norm in New Mexico and the privately owned utility is more than happy to encourage this partial rebate to increase tap-ons to their systems.

Each of the non-cost factors (Table 5.3) used to help sell the public on the wisdom of the purchase of Epcor’s Edgewood water system is very debatable or is completely wrong in the assumptions. The source of these assumptions and the grading was “town personnel” who apparently approved the report’s \$35,000 price tag without consulting the town council. It is hardly objective. The consultant states that he had discussions with individuals knowledgeable of the existing water system. I was surprised that I had not received any indication from anyone involved in this study. I was the development consultant for the owners and developers of Rancho Sandia, Windmill Ranch, Bella Vista Units “F” and “G” on Windmill Road, Tranquil Valley, and was the developer of Chamisa Ranch, all on the Epcor system, and granted easements or wrote most of the checks to pay for the 12” water line along Walker Road, all expenditures for the main Juniper Hill tanks and 8” mains which replaced 3” mains to those tanks, and many other line projects which profoundly improved the Edgewood water utility today owned by Epcor. Thus I have been intimately familiar with the water utility throughout its history. I am the owner of ReMax Western Heritage, a real estate company in Edgewood doing business here for 46 years.

The Town has also contracted for a “preliminary” valuation document from R.E. Pender, Inc., which cannot be relied upon in any manner. The drafter makes many disclaimers about a lack of necessary information, assumes the systems evaluated lie entirely within the Town of Edgewood, which they do not, lacks any inventory of just what the system contains, what property ownership and water rights are included, and he ends the report with a page full of question marks. It is this type of underevaluation that has gotten the El Dorado water district and many other small systems that took the condemnation route, in such dire financial trouble.

I respectfully submit these comments for the council’s and mayor’s consideration and strongly recommend the town drop the project of buying the Epcor water system as it is a very poor and risky investment and would saddle the citizens of Edgewood with excessive high risk debt and a profound

possibility of future default. I have recently had conversations with former councilor Ring and former councilor Simmons, and they were under the mistaken assumption that buying the water system was for the expressed goal of bailing out the sewer system. Both the town clerk and the PER consultant have stated that state law requires the two systems must be self supporting and apparently cannot commingle their funds. I have no idea why that rumor was started and by whom but it is obvious that the failing sewer system cannot be saved by ownership of the water system.