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Acting State Comptroller

September 21, 2021

VIA EMAIL AND U.S. MAIL

Honorable Lisa Jampetti
Mayor, Egg Harbor City
500 London Avenue
Egg Harbor City, NJ 08215-1599

Re: OSC # 21-501 Sale of Water and Wastewater Systems by Egg Harbor City

Dear Mayor Jampetti,

On or about April 1, 2021, the Office of the State Comptroller ("OSC") became aware of an Agreement between Egg Harbor City ("EHC") and a buyer, ("Buyer") ("Agreement") for the proposed sale of EHC's water and wastewater systems ("Systems") at a purchase price of \$21,800,000 pursuant to the New Jersey Water Infrastructure Protection Act, *N.J.S.A. 58:30-1 et seq.* ("WIPA").

In accordance with OSC's statutory authority, by letter dated April 1, 2021, OSC notified EHC of its failure to comply with *N.J.S.A. 52:15C-10(b)* and requested the proposed Agreement and other documentation required by WIPA in connection with the sale of the Systems. EHC acknowledged it failed to submit the request for qualifications and for proposals to OSC for review prior to their issuance as required by *N.J.S.A. 52:15C-10(b)*.

OSC notes that EHC cooperated fully with OSC's requests and provided full disclosure of the actions it took to comply with WIPA. As described below, however, OSC's review of the requested documents found irregularities and instances of non-compliance with WIPA and applicable regulations. A version of this letter was shared with EHC to provide it with an opportunity for comment. OSC considered EHC's August 24, 2021 response to that letter and modified this letter as appropriate in response to those comments.

I. Background

Enacted in 2015, WIPA permits municipalities to sell their water supply and wastewater treatment systems to a private or public entity without a public referendum if emergent conditions exist, as defined in *N.J.S.A. 58:30-5(b)*. EHC is the first municipality to use WIPA to sell its

Systems. On April 1, 2021, OSC issued a letter to EHC advising that OSC had become aware of the pending Agreement. OSC's letter requested documents demonstrating compliance with WIPA and noted that all contracts valued at \$12.5 million or greater require OSC review prior to advertising the solicitation. In response to OSC's April 1st letter, EHC submitted a letter dated April 5, 2021, acknowledging its failure to comply with *N.J.S.A. 52:15C-10(b)*. Along with the April 5th letter, and in response to additional OSC inquiries, EHC submitted numerous documents to OSC, including:

- January 4, 2016 agreement between EHC and its municipal engineer (hereinafter referred to as "City Engineer") appointing the firm as its municipal engineer for three years;
- March 30, 2017 proposal from the City Engineer to complete a Water and Sanitary System Infrastructure Assessment, Rate Study and Asset Valuation Analysis with an estimated fee of \$41,600;
- November 27, 2018 letter from the City Engineer in its capacity as municipal engineer, to the New Jersey Department of Environmental Protection ("DEP") of EHC's intent to commence the WIPA process;
- December 6, 2018 "Emergent Condition Evaluation Report" by the City Engineer;
- December 27, 2018 EHC Resolution formally accepting the findings and determinations made in the Emergent Condition Evaluation Report dated December 6, 2018 by the City Engineer;
- January 2019 agreement between EHC and the City Engineer appointing the firm as its municipal engineer for another three years;
- January 10, 2019 letter from the City Engineer to DEP notifying DEP of EHC's approval of the Emergent Condition Evaluation Report in which the City Engineer identified the existence of two emergent conditions and "completed an extensive review of both systems, determined the value of the systems, compiled a capital improvements plan to quantify required maintenance and the associated costs, and completed an operations analysis and rate study to determine the impact that the said improvements will have on the city and the consumer.";
- January 28, 2019 advertisement order confirmation from the Press of Atlantic City of EHC's notice of the WIPA public hearing;
- February 28, 2019 resolution signed by the EHC Mayor, EHC Council President and the City Engineer certifying the existence of two emergent conditions as identified in the City Engineer's Emergent Condition Evaluation Report;
- Supplemental financial documentation prepared by EHC's Chief Financial Officer requested by DEP;
- April 25, 2019 DEP determination letter as to the existence of emergent condition set forth in *N.J.S.A. 58:30-5(b)(5)*;
- September 16, 2019 proof of re-advertisement of EHC's Request for Qualifications (RFQ) for the sale or lease of its assets under WIPA;
- November 21, 2019¹ letter from the City Engineer to EHC recommending that all three respondents to the RFQ are qualified to receive a request for proposals;

1. OSC notes the date on the letter as "November 18, 2011" appears to be a typographical error.

- January 2020 Request for Proposals - Sale of Water and Wastewater Utility Systems issued by EHC;
- May 28, 2020 EHC resolution naming the Buyer as the designated respondent, and authorizing negotiation of the sale or lease agreement with the vendor pursuant to WIPA; and
- January 21, 2021 draft Agreement between EHC and the Buyer for the sale of the Systems.

II. Findings

A. Allowing the City Engineer to provide the emergent conditions report required under *N.J.S.A. 58:30-5(a)* and *(b)* and also provide the independent financial advisor report required under *N.J.S.A. 58:30-5(c)* failed to account for the independence of the financial advisor’s analysis required by WIPA.

Among other things, the WIPA statute requires: (1) a determination by the mayor, the mayor’s designee of the municipality and a licensed engineer that at least one emergent condition exists as described in *N.J.S.A. 58:30-5(b)*, and (2) a report on the value of the system prepared by an independent financial advisor informing the municipality and the public of the short and long term impacts to rate-payers of the proposed transaction and that provides an estimate of the financial requirements to address the emergent conditions and operation and maintenance of the system, pursuant to *N.J.S.A. 58:30-5(c)*.

Under WIPA, the licensed engineer² and the independent financial advisor are responsible for separate and distinct steps in the proposed sale of the water asset. Pursuant to *N.J.S.A. 58:30-5(a)*, a licensed engineer is responsible for making a determination that at least one of the emergent conditions listed in *N.J.S.A. 58:30-5(b)* exists. After that determination has been made, the municipality must retain an independent financial advisor to conduct a financial analysis of the proposed transaction. Significantly, the “independent” nature of the “financial advisor” indicates that the financial advisor should be free from the influence or control of others. *See N.J.S.A. 58:30-5(c)*. The financial advisor required by WIPA has a different purpose than the licensed engineer: the advisor is responsible for conducting a financial analysis of the proposed transaction and presenting its findings to the municipality. To move forward under WIPA, the municipality must conduct a public hearing to present the findings regarding the certification of emergent conditions, as well as the independent financial advisor’s findings. *N.J.S.A. 58:30-5(d)*.

Here, the City Engineer prepared and submitted an “Emergent Condition Evaluation Report” which identified the existence of two emergent conditions under WIPA. By Resolution dated December 27, 2018 EHC’s Common Council accepted the City Engineer’s report. The Mayor, EHC’s Council President and the City Engineer made the determination of the existence of two emergent conditions on February 29, 2019. The City Engineer also conducted a financial analysis of the Systems and provided EHC with a valuation of the same, a capital improvements plan to quantify required maintenance and associated costs, an operations analysis, and a rate study to determine the impact on ratepayers if the Systems were retained by the municipality.

² Pursuant to *N.J.S.A. 58:30-3*, “Licensed engineer” is defined as a “professional engineer licensed pursuant to P.L. 1938, c. 342 (C.45:8-27 et seq.)”

Collectively, these reports were relied upon by EHC and submitted to DEP as the independent financial advisor's report.

The plain language of WIPA contemplates two separate and distinct roles in the WIPA process: a licensed engineer to report on the condition of the water asset and an independent financial advisor to assess its value. The independent nature of the financial advisor is further evidenced by the fact that its report is due after the emergent conditions are certified by the municipal engineer, thereby providing a measure of protection for the public when a water asset is sold without a public referendum.

Without reference to legislative statements supporting its assertion, EHC argues the intent of the Legislature was to require "the financial advisor be independent of the municipality, not from the Engineer." EHC asserts that the term "independent" was meant to indicate someone who is not an employee of the City. EHC contends, "[a]ny firm performing a service for the City would have a contractual relationship with the City and, therefore, have the same fee-for-service relationship with the City." As a result, that firm would be independent from EHC "as any non-employee being paid by the City to perform a service." Under EHC's view, any entity, including an entity with a longstanding professional relationship with EHC earning substantial income from the municipality and involved, possibly daily, in advising the municipality, could be "independent." In our view, the requirement of independence cannot be so easily met.

In the absence of a court decision or administrative interpretation of WIPA, OSC is left to interpret the statute on its own. Any reasonable test for independence must consider whether any existing financial or other relationship would cause a reasonable person to doubt that the opinion offered by the financial advisor was objective and free of bias. An engineering firm with an existing relationship to a municipality, that participated in other parts of the municipality's WIPA application, and seeks on an ongoing basis to remain as the contracted municipal engineer cannot reasonably be viewed as independent. Here, the City Engineer has had, and continues to enjoy, a long-standing contractual relationship with EHC, and also completed a majority of EHC's WIPA application. By comparison, a financial advisor who has not previously been retained by or in the employ of a municipality and who has one, and only one, task to perform for the municipality is truly independent. Such a person can serve as a check on the proposed sale of the asset and can provide a detached opinion regarding the impact of the sale on rate-payers for both the short and long term. The independence of the financial advisor is especially important under WIPA because the sale is not subject to a referendum.

Allowing the City Engineer to "wear both hats" negates the independence required under WIPA for the financial analysis and denies the governing body and the public at large the opportunity to review a report from an expert in financial matters who is detached from the proposed sale of important public infrastructure.

EHC advised OSC it would not take any corrective action regarding this concern because the proposed Buyer obtained two appraisals within 7% of the valuation performed by the City Engineer. Appraisals commissioned for the benefit of the Buyer, which has a clear self-interest and is not charged with protecting the interests of rate-payers, however, should not be substituted as independent financial reports for the benefit of EHC or the rate-payers.

B. EHC did not procure the services of an independent financial advisor in accordance with the Local Public Contracts Law.

Notably, the legislature requires a municipality to retain the services of an independent financial advisor through the utilization of applicable procurement laws. *N.J.S.A.* 58:30-5(c). The phrase, “through the utilization of applicable procurement laws” demonstrates an additional level of separation between the licensed engineer and the independent financial advisor. *Ibid.* As noted, above, EHC asserts this language was included by the Legislature to ensure that the financial advisor was independent of the municipality and, therefore, does not preclude a municipality from using its municipal engineer as the independent financial advisor. As described below, however, EHC did not follow the Local Public Contracts Law (*N.J.S.A.* 40A:11-1 *et seq.*, “LPCL”) when it utilized the City Engineer to provide financial analyses for the proposed sale of the Systems.

OSC requested documents from EHC regarding the procurement process for the independent financial advisor required by WIPA. In response, OSC was advised that a licensed engineer employed by the City Engineer performed this function for EHC. The records submitted to OSC indicate EHC procured the services of the City Engineer to serve as its municipal engineer pursuant to *N.J.S.A.* 19:44A-20.7, commonly referred to as the “fair and open” procurement process, and awarded the City Engineer a three-year contract in January 2016 and again in January 2019. Under these agreements, the City Engineer provided engineering, planning, surveying and contract operations services, but not financial advisory services.

EHC also provided OSC with the City Engineer’s proposal in the amount of \$41,600 for a Water & Sanitary System Infrastructure Assessment, Rate Study & Asset Valuation Analysis, dated March 30, 2017. The scope of work in the proposal includes the preparation of a “20 Year Capital Improvement Plan,” taking into account the current utility operating budget and current debt service and “a valuation of the existing assets to assist in age versus useful life expiration and replacement.” Even though these services were not included in the scope of work for the municipal engineering agreement and their cost exceeded the bid threshold,³ EHC did not solicit competitive proposals as required by the LPCL. Because engineering services are considered professional services under the LPCL, such contracts may be awarded without formal bidding. However, financial advisory services are not exempt from bidding as a professional service, because they do not satisfy the definition of professional services⁴ under the LPCL. Therefore, the financial advisory services contemplated by WIPA should have been procured after public advertising of a bid pursuant to *N.J.S.A.* 40A:11-4, or a request for proposals as authorized by *N.J.S.A.* 40A:11-4.1(m).

³ Pursuant to *N.J.S.A.* 40A:11-3, between July 1, 2015 and June 30, 2020, the bid threshold was \$40,000.

⁴ Pursuant to *N.J.S.A.* 40A:11-2(6), “Professional services’ means services rendered or performed by a person authorized by law to practice a recognized profession, whose practice is regulated by law, and the performance of which services requires knowledge of an advanced type in a field of learning acquired by a prolonged formal course of specialized instruction and study as distinguished from general academic instruction or apprenticeship and training. Professional services may also mean services rendered in the provision or performance of goods or services that are original and creative in character in a recognized field of artistic endeavor.”

In its response to OSC, EHC asserts that the City's procurement of engineering services complied with *N.J.S.A.* 40A:11-4.1(m), however no documentation supports this assertion. Here, EHC seems to confuse a "fair and open" solicitation as permitted by *N.J.S.A.* 19:44A-20.7 with competitive contracting under the LPCL.

C. The proposed Agreement is missing certain provisions required by WIPA.

The proposed Agreement failed to include required provisions under the Act. Specifically, the Agreement does not include a clause, as required by *N.J.S.A.* 58:30-7(b)(1), stating "that to the extent it does not violate any existing collective bargaining agreements between the capable private or public entity and its employees, the capable private or public entity shall give first consideration in hiring to any public employees displaced by the long-term lease or sale of the water or waste water assets."

In addition, the Agreement must require that, in the performance of the Agreement, the Buyer of the Systems agrees to: (1) pay workers not less than the prevailing wage and employ workers from an apprenticeable trade in accordance with *N.J.S.A.* 34:11-56.25 et seq; and (2) require that all contractors and subcontractors comply with the Public Works Contractor Registration Act, *N.J.S.A.* 34:11-56.48 et seq.

EHC has agreed to amend the Agreement to include these statutorily required provisions.

III. Conclusion

OSC will monitor and retain oversight of the proposed Agreement through the completion of the WIPA process. To that end, EHC shall provide OSC notice of its submission of: (1) the proposed Agreement to the Board of Public Utilities ("BPU") and evidence of BPU's determination as required under *N.J.S.A.* 58:30-7(b); and (2) the proposed use of the sale proceeds to the Director of the Division of Local Government Services and evidence of the Director's disposition of EHC's submission in accordance with *N.J.S.A.* 58:30-(c)(6). Finally, prior to EHC's approval of the Agreement pursuant to *N.J.S.A.* 58:30-8, EHC shall provide OSC with the proposed Agreement, with any revisions required by BPU or as may be agreed to by the parties.

Compliance with all applicable statutory requirements is vital to protecting taxpayer funds, encouraging free and fair competition, and ensuring government efficiency and transparency. These principles enable New Jersey residents to trust public officials are making well-reasoned and unbiased decisions that best serve their public health and financial interests.

Through this letter, we advise the public and other state agencies involved in WIPA reviews of EHC's failure to notify OSC of this procurement in violation of *N.J.S.A.* 52:15C-10(b). Under normal circumstances, if a municipality seeking to sell infrastructure under WIPA had not complied with the statutory requirement to procure an independent financial advisor, OSC would decline to approve the procurement during a pre-advertisement review. Here, that opportunity was denied because EHC, in violation of law, proceeded with the procurement without first seeking OSC's approval.

In the absence of EHC voluntarily addressing the concern regarding the financial advisor's independence, and the underlying procurement issue, it is not clear what will happen. No agency involved in WIPA reviews has been given explicit authority to ensure that the financial advisor is independent and, thus, that an objective, unbiased financial analysis has been conducted and made available to council members and affected rate-payers before the governing body hears public input and votes to proceed with a WIPA sale. The Board of Public Utilities and Department of Community Affairs may consider this issue and require it to be addressed, but those agencies in the first instance must decide what components of WIPA are within their jurisdiction and we do not prejudge that issue.

It may also be appropriate for the Legislature to consider amending WIPA to identify a single state agency to be responsible for ensuring the integrity of the process for selling the public asset from beginning to end. Currently, three state agencies each review a component of the WIPA process at different points in the process. OSC's review of EHC's proposed sale brought to light that no one state agency is charged with ensuring the financial impacts of the sale have been analyzed and reviewed by an independent expert. Even if timely submitted, OSC's pre-advertisement review of a request for qualifications seeking a buyer for the public asset would occur after council and public review of the financial advisor's report and the period for a public petition to require a referendum has lapsed. In view of the permanence of a sale of municipal infrastructure, and of the Legislature's effort to ensure public participation by residents impacted by the sale, a review at the state level of the process for initiating a WIPA sale may be appropriate.

Respectfully,

KEVIN D. WALSH
ACTING STATE COMPTROLLER

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