



OFFICE OF THE CITY AUDITOR COLORADO SPRINGS, COLORADO

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15-27 Multiyear Water Rate Follow Up

October 2015

Purpose The purpose of this audit was to update the actual and projected costs and rate impacts of the Southern Delivery System (SDS) as compared to historical multiyear water rate increases. Previous reports were issued as part of the water rate filing cases in 2010 and 2012.

Conclusion:

Southern Delivery System (SDS) program costs will be lower than forecasted in 2010. The cash used for SDS has exceeded the new revenue generated from the rate increases during the multiyear period of 2011—2014. There were no recommendations made as a result of this audit.

The Southern Delivery System (SDS) program is a multiyear water construction project, which the Office of the City Auditor (OCA) has been auditing since 2009. In late 2009, Colorado Springs Utilities proposed the concept of a multiyear water rate increase to assure revenues would be available to pay for SDS. The original plan was to issue 40 year bonds for approximately \$870 million of the total program cost, including debt funding of interest during construction. Annual rate increases of 12% per year beginning in 2011 and continuing through 2016 were anticipated.

The initial two year rate increase of 12% per year was approved and became effective on January 1, 2011 and 2012. Additional rate increases of 10% per year were implemented effective January 1, 2013 and 2014.

As a follow up to our previous work, this audit updated the actual costs for the program to date plus the anticipated costs to complete as of December 2014. We also analyzed the actual revenue received from the multiyear rate increases and the impact on rates from SDS. The cost of SDS was reviewed in 2010, 2012 and as of December 2014.

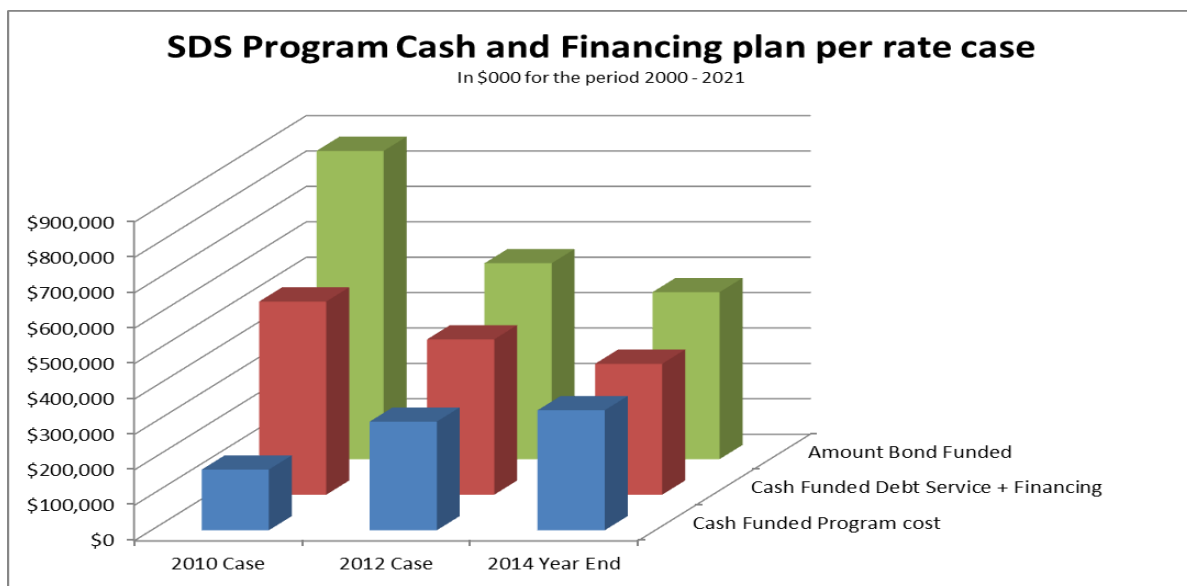
How much will SDS cost and how will we pay for it?	Projected costs and finance plan changes over time For costs incurred during 2000—2021 (in \$000)		
	2010 Rate Case	2012 Rate Case	2014 Year End
Total Projected SDS Costs*	\$1,587,760	\$ 1,298,870	\$ 1,180,093
Bond Funded	\$ 870,688	\$ 553,260	\$ 471,588
Cash Funded Program Costs	\$ 171,443	\$ 306,850	\$ 338,990
Cash Funded Financing Cost	\$ 545,629	\$ 438,760	\$ 369,515

*Total SDS Costs include all capital expenditures, land, regulatory assets, O&M, applied overhead and financing costs including debt service during the period 2000—2021.

15-27 MULTIYEAR WATER RATE FOLLOW UP

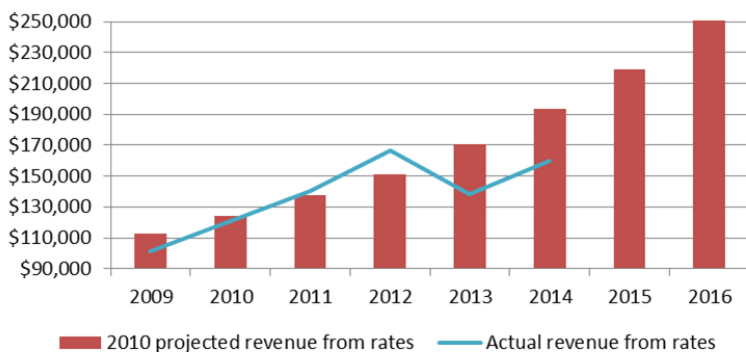
Since 2010, total anticipated Southern Delivery System costs have decreased by \$408 million, or 25.7%. This decrease includes actual and projected capital expenditures, land acquisition, overhead, operations costs, maintenance costs, regulatory assets, financing and debt service from 2000 through 2021. The corresponding reduction in projected total bond funding for SDS from 2010 to 2014 was \$399 million or 45.8%. Debt service refers to payments of principal and interest on outstanding long term bonds. Because of the reductions in projected program cost and financing, the annual debt service payments for SDS bonds will be \$26 million lower than the initial projections in 2010. These changes will increase cash requirements of the project in the short term offset by long term savings in debt service payments of approximately \$1.15 billion over the life of the bonds.

To pay for SDS, a combination of debt financing and cash was used. The approach to paying for SDS has changed significantly since the 2010 multiyear rate case. Initial planning anticipated greater reliance on long term debt to finance the program. Program costs projected to be bond financed fell \$399 million from the 2010 to the 2014 forecast. The planned use of cash for construction increased while cash used for financing decreased leaving total SDS cash requirements relatively flat over that same time period.



Projected and Actual Water Revenue

in \$000



In the 2010 Office of City Auditor rate review, \$383 million was anticipated to be generated by the multiyear rate increases and \$739 million would be generated from the base rates during the period 2011 through 2016⁽¹⁾. Actual revenues generated since 2011 have not been as high as forecast. Actual revenue collected during 2011—2014 was \$47 million lower than projected in the original multiyear rate case.

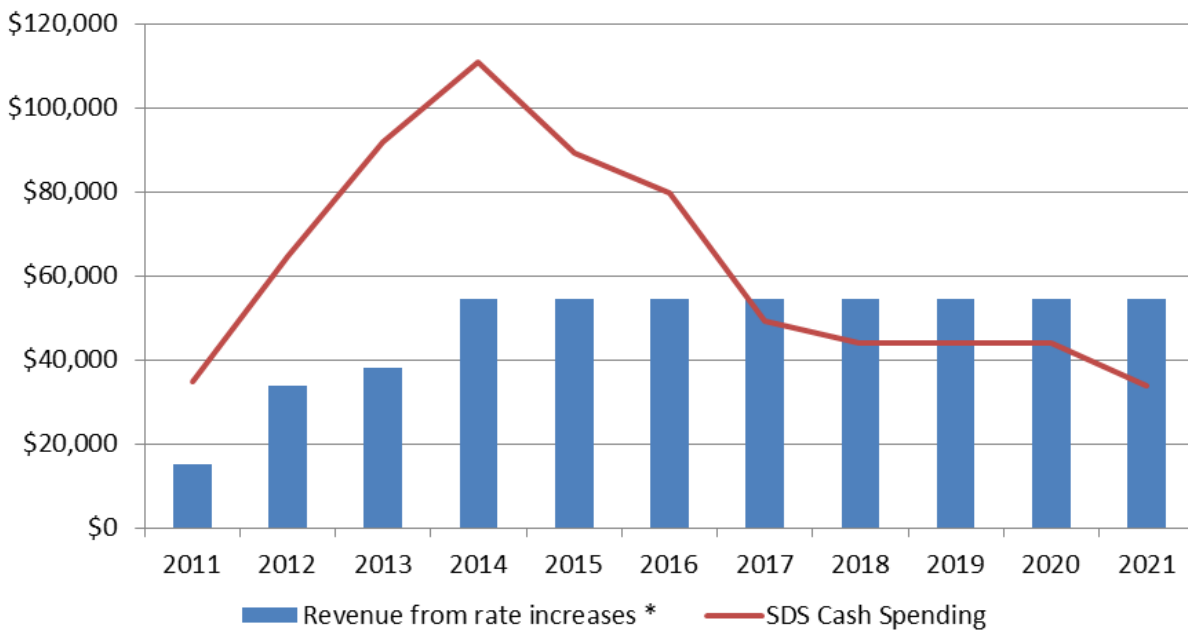
⁽¹⁾ In 2009, water rates increased approximately 40% over 2008. Utilities indicated the major drivers for this increase was a reduction in contributions-in-aid, an increase in operations and maintenance expenses, and an increase in debt service. The revenues from the 2009 rate increase are not included in this review of revenues from SDS related rate increases and cash uses.

15-27 MULTIYEAR WATER RATE FOLLOW UP

The multiyear water rate increases were intended to provide funding to pay for the SDS program. We reviewed the cash requirements of the program and compared them to the new revenue that has been generated from those rate increases in 2011—2014. As the chart below shows, the cash funding of SDS have exceeded the new revenue generated from the rate increases.

In 2010, it was projected that 78% of the new revenue from rate increases would be used by SDS and the remainder would be available for use by the general water system. As of the 2012 rate case, the percentage of SDS cost to be financed using long term debt had started to change and more of the capital costs were planned to be cash funded. Given the projected sales volumes, revenue forecasts, and reduced program costs, rate increases were reduced from the initial projections. Ultimately, the multiyear increases were implemented as two years of 12% increases followed by two years of 10% increases, rather than six years of 12% increases as originally envisioned. However, since the 2012 rate case, revenues have not met projections and more cash has been used on SDS, leaving less available for other parts of the water system.

**Revenue from multi-year water rate increases vs. SDS cash spending
(in \$000)**



**Future revenue assumes no additional rate increases*