



# OFFICE OF THE CITY AUDITOR PUBLIC REPORT

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Date: June 20, 2012  
To: President of Council Hente, President Pro-Tem Martin, and Members of City Council  
Re: 12-13 Multiyear Water Rate Case

We have reviewed the 2013-2014 Water Rate Case filing including cost of service studies, financial forecasts and the Southern Delivery System (SDS) rate impact. The filings are scheduled to be heard during a Public Hearing on June 26, 2012.

## **Conclusion**

We conclude that the proposed rate increases for 2013 and 2014 are properly supported by the financial forecast and the Cost of Service Study (COSS) provided. Projected costs for SDS were properly reflected and included in the revenue requirements. Additionally, we conclude that the COSS used to determine rates to be charged by customer class was accurate and materially consistent with prior methodology. We have one observation for consideration in future reviews.

## **Purpose and Scope**

Our review focused on the accuracy and consistency of the methodology used to develop the proposed rate changes. The cost of service studies were examined for each rate for achievement of objectives, compliance with the tariff, and agreement to the appropriate source documentation.

The 10 Year Long-Term Financial Forecast (LTFF) is used by Colorado Springs Utilities to prepare the Annual Operating Plan and determine the revenue requirement for rate cases. Once the revenue requirement is known, the Cost of Service Study is used to determine how the revenue requirement will be distributed among the rate classes. We reviewed the LTFF for 2013 and 2014 to determine if water system costs including the Southern Delivery System (SDS) were incorporated into the rate case accurately and consistently. The impact of SDS on the proposed rate increase and the financial metrics for the enterprise were reviewed.

## **Savings Due to Change in Project Funding**

SDS is a multiyear construction project with Phase 1 expected to be complete in 2016. A significant portion of project spending is scheduled to take place during 2013-2014. The majority of funding for SDS interest expense was previously planned for and achieved through debt funds. Effective January 2012 SDS interest expense during construction was changed from funding by debt to cash funding. The percentage of project costs funded by debt was also reduced.

We recognize Colorado Springs Utilities positive efforts to date to effectively manage project costs. The total forecasted budget for SDS has been reduced by approximately \$47,000,000 due to actual and projected savings in design and construction costs compared to earlier estimates. The strategic changes mentioned above, coupled with historically low interest rates, resulted in reduced total debt funding for SDS through 2016 from \$864,288,000 in the previous forecast to \$553,260,000. These changes will increase cash requirements of the project in the short term in favor of long term savings in debt service payments of approximately \$700,000,000.



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## Observation and Recommendation:

### Observation

Colorado Springs Utilities proposed a *New Rate Option – Large Nonseasonal Rate* in this rate filing. This rate is listed in the Rate Report, tariff sheets and Resolution for approval; however it was not included in the COSS. Therefore, we could not review this proposed rate and its impact to other rate customers. The Large Nonseasonal Rate will be a lowered rate to nonresidential customers with large volumes and stable annual water usage. Not including this rate in the COSS is consistent with the Electric Large Power and Light pilot rate offered in 2008.

### Recommendation

We recommend Colorado Springs Utilities prepare a detailed 2015 Water Cost of Service Study in 2014 and provide this study to the Office of the City Auditor for review whether or not a rate change is proposed. This study should include evaluation of the Large Nonseasonal Rate impact to other rate customers and the impact of SDS saving on future revenue requirements.

### Management Response

Colorado Springs Utilities agrees with the Office of the City Auditor's recommendation.

We conclude overall the 2013-2014 Water Rate Case filing was properly supported by the cost of service study and the methodology used was consistent and accurately applied.

Please contact me if you have any questions regarding this report. I plan to attend the rate hearing on June 26.

Respectfully,

A handwritten signature in black ink, appearing to read "Denny L. Nester".

Denny L. Nester, MBA CPA CIA CFE CGFM CGAP  
City Auditor

cc: Jerry Forte, Chief Executive Officer  
Bill Cherrier, Chief Financial Planning and Financial Officer  
Dede Jones, General Manager, Financial Services  
Stella Chan, Manager, Financial Planning and Pricing  
Steve Berman, Manager, Financial Forecasting, Reporting and Budgeting  
Dave Maier, Manager, Enterprise Risk Management  
Henry Henderson, Pricing and Forecasting Supervisor