

**COLORADO SPRINGS UTILITIES**

(An Enterprise Fund of the  
City of Colorado Springs, Colorado)

**FINANCIAL STATEMENTS**

Including Independent Auditors' Report

As of and for the Years Ended December 31, 2013 and 2012

# COLORADO SPRINGS UTILITIES

(An Enterprise Fund of the  
City of Colorado Springs, Colorado)

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## INDEPENDENT AUDITORS' REPORT

To the Audit Committee  
Colorado Springs Utilities  
Colorado Springs, Colorado

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Colorado Springs Utilities, an enterprise fund of the City of Colorado Springs, Colorado, as of and for the years ended December 31, 2013 and 2012, and the related notes to the financial statements, as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control over financial reporting relevant to Colorado Springs Utilities' preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Colorado Springs Utilities' internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

To the Audit Committee  
Colorado Springs Utilities

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Colorado Springs Utilities as of December 31, 2013 and 2012, and the changes in its financial position and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

### **Emphasis of Matters**

As discussed in Note 1, the financial statements present only the Colorado Springs Utilities enterprise fund and do not purport to, and do not, present fairly the financial position of the City of Colorado Springs, Colorado, as of December 31, 2013 and 2012 and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 2, Colorado Springs Utilities adopted the provisions of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, effective January 1, 2013. The prior year has been restated for this change. Our opinion is not modified with respect to this matter.

As discussed in Note 2, Colorado Springs Utilities adopted the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, effective January 1, 2012. Our opinion is not modified with respect to this matter.

### **Other Matter**

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Schedule of Funding Progress information as listed in the table of contents be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we will also issue a report on our consideration of Colorado Springs Utilities' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Colorado Springs Utilities' internal control over financial reporting and compliance.

*Baker Gilly Vichow Krause, LLP*

Madison, Wisconsin  
April 14, 2014

# COLORADO SPRINGS UTILITIES

## MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

### INTRODUCTION

The following Management's Discussion and Analysis ("MD&A") serves as an introduction to the financial statements of Colorado Springs Utilities ("Utilities"). It is intended to be an objective and easily readable analysis of significant financial and operating activities and events for the fiscal years ended December 31, 2013, 2012 and 2011. It also provides an overview of Utilities' general financial condition and results of operations. The financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") as applied to units of local government and promulgated by the Governmental Accounting Standards Board ("GASB").

Utilities is an enterprise fund of the City of Colorado Springs, Colorado ("City") that provides electric, streetlight, natural gas, water and wastewater services (the "Utility System"), to customers in the Pikes Peak region. The organization operates an electric generation, transmission, and distribution system; a streetlight system; a natural gas distribution system; a water collection, treatment and distribution system; and a wastewater collection and treatment system. Utilities' service area includes the City, Manitou Springs and many of the suburban residential areas surrounding the City. The military installations of Fort Carson Army Base, Peterson Air Force Base, Cheyenne Mountain Air Force Station and the United States Air Force Academy receive electric service, natural gas supply and transportation service and water service from Utilities, and Peterson Air Force Base also receives wastewater treatment service. The City is currently the primary customer of the streetlight system and is responsible for the majority of streetlight service charges.

Utilities' financial statements do not purport to, and do not present the financial position of the City, component units or its joint ventures as of December 31, 2013 and 2012, nor the changes in its financial position and its cash flows, where applicable, for the years then ended in conformity with U.S. GAAP. The MD&A includes known information that management is aware of through the date of the auditors' report. Please read this MD&A in conjunction with Utilities' financial statements and accompanying notes that follow this section.

### BASIC FINANCIAL STATEMENTS

#### *FINANCIAL STATEMENTS*

Utilities' annual report includes three financial statements with accompanying notes that are an integral part of these statements. The basic financial statements include: 1) Statements of Net Position, 2) Statements of Revenues, Expenses and Changes in Net Position and 3) Statements of Cash Flows. Comparative total data for prior year has been presented in order to provide an understanding of changes in Utilities' financial position and operations. Certain amounts presented in the prior year's data have been reclassified in order to be consistent with the current year's presentation.

**Statements of Net Position** - This statement reports net position as the difference between 1) assets and deferred outflows of resources and 2) liabilities and deferred inflows of resources as of the end of each fiscal year. Assets are separated into current and noncurrent categories and are reported in the order of liquidity. Deferred outflows of resources are the consumption of net assets in one period that are applicable to future periods. Liabilities are segregated into current and noncurrent categories. Deferred inflows of resources are the acquisition of net assets that are applicable to future reporting periods. The components of net position are classified as net investment in capital assets, restricted collateral, restricted debt service, restricted health care benefits, restricted categories for other purposes or unrestricted.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

**Statements of Revenues, Expenses, and Changes in Net Position** - This statement measures the activities for the year and can be used to determine whether the rates, fees and other charges are adequate to recover expenses. All revenues and expenses are accounted for in this statement for the year ended December 31.

**Statements of Cash Flows** - This statement reports all cash receipts and payments summarized by net changes in cash from operating, noncapital financing, capital and related financing and investing activities for the year ended December 31. This statement is prepared using the direct method, which reports gross cash receipts and payments, and presents a reconciliation of operating income to net cash provided by operating activities. This statement also separately lists the noncash financing and investing activities.

**Notes to the Financial Statements** - Notes to the financial statements provide additional detailed information and required disclosure in support of the financial statements.

### COMPONENT UNITS AND JOINT VENTURES

#### COMPONENT UNITS - CITY

**Public Authority for Colorado Energy ("PACE")** - PACE is a nonprofit corporation that has been organized by the City for the purpose of assisting the City by acquiring, financing and supplying natural gas for Utilities. On June 27, 2008, the City (on behalf of Utilities) entered into a Natural Gas Supply Agreement with PACE. Utilities will purchase approximately 20.0% of Utilities' natural gas supply needs for 30 years through a natural gas prepayment transaction among PACE, Merrill Lynch Commodities, Inc., Bank of America Corporation and Royal Bank of Canada.

**Fountain Valley Authority** - Utilities has a 71.4% interest in this authority, which is a political subdivision of the State of Colorado, formed primarily to construct a water treatment plant and to operate the water treatment plant and water conveyance system for its five customers.

**Aurora-Colorado Springs Joint Water Authority** - Utilities has a 66.7% participation share in this authority, which is a political subdivision of the State of Colorado, formed for the purpose of developing water resources, systems or facilities for the benefit of Utilities and the City of Aurora, Colorado.

**Canal and Reservoir Companies** - Utilities has interests ranging from 51.9% to 77.2% in four canal and reservoir companies. This ownership interest represents proportionate ownership and control of the companies' facilities and water rights. The water rights add significant physical water to the water supply portfolio in addition to allowing for exchange, storage, staging and delivery of Utilities' water supply.

#### JOINT VENTURES

**Young Gas Storage Company Ltd.** - Utilities has an equity interest of 5.0% in this joint venture, organized to develop and operate a natural gas storage system near Fort Morgan, Colorado.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### SIGNIFICANT EVENTS

**Colorado Wildfires and Flooding** - Utilities continues to address the risk of wildfires and related flooding. While a number of wildfires occurred in 2013 in areas near Colorado Springs, Utilities' assets and operations were not directly impacted.

In September 2013, significant rainfall and flooding occurred in Utilities' service and surrounding areas. Customer outages reported were short in duration and in all material aspects, Utilities' systems functioned properly. Utilities continues to evaluate the impact to its Utility System. A preliminary estimate of the costs to repair or replace damaged infrastructure is \$1.7 million, excluding watershed remediation. Utilities is working with government agencies to potentially recover some or all of its costs.

The Waldo Canyon fire that burned in 2012 significantly impacted Utilities. In late July 2012, rainfall occurred over the burn area of this fire resulting in direct damage to watershed assets requiring Utilities to engage in flood remediation to mitigate future damages. The combined costs to repair damages to watershed assets, to mitigate potential damages from future flooding, to repair and replace certain assets of Utilities, to fight the fire, to restore service and to manage operations are estimated at \$18.7 million. Approximately \$5.0 million in federal grant funds have been secured to defray the costs of ongoing flood mitigation and containment projects in the Northfield Watershed area of operations. Utilities is in negotiation with its insurance carrier with respect to recoverable damages. Regarding the Waldo Canyon fire and the subsequent flood event, approximately \$1.2 million has been recovered from insurance to date. A final estimate of recoverable insurance proceeds is not available at this time.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### CONDENSED FINANCIAL STATEMENTS

Condensed financial statements with comparative information as of December 31:

#### CONDENSED STATEMENTS OF NET POSITION

	2013	2012	2011*
		(in thousands)	
<b>Assets and Deferred Outflows of Resources</b>			
Assets			
Current assets	\$ 427,938	\$ 379,484	\$ 290,279
Other noncurrent assets	299,821	339,707	402,008
Capital assets, net	3,388,201	3,204,036	3,061,793
Total Assets	4,115,960	3,923,227	3,754,080
Deferred outflows of resources	78,035	299,719	259,129
Total Assets and Deferred Outflows of Resources	\$ 4,193,995	\$ 4,222,946	\$ 4,013,209
<b>Liabilities, Deferred Inflows of Resources and Net Position</b>			
Liabilities			
Current liabilities	\$ 182,657	\$ 179,175	\$ 212,838
Noncurrent liabilities	2,522,965	2,527,208	2,460,954
Total Liabilities	2,705,622	2,706,383	2,673,792
Deferred inflows of resources	2,375	63,207	4,983
Total Net Position	1,485,998	1,453,356	1,334,434
Total Liabilities, Deferred Inflows of Resources and Net Position	\$ 4,193,995	\$ 4,222,946	\$ 4,013,209

\* 2011 data was not adjusted for GASB Statement No. 65 conformance.

#### Assets

*Current assets* increased in 2013 and 2012 by \$48.5 and \$89.2 million, respectively. The increase during 2013 is primarily due to an increase of \$48.6 million in unrestricted investments. The increase during 2012 is primarily due to increases in the following: \$56.5 million in unrestricted cash and cash equivalents, \$10.5 million in restricted cash and cash equivalents and \$24.0 million in unrestricted investments.

*Other noncurrent assets* decreased \$39.9 and \$62.3 million during 2013 and 2012, respectively. The decrease is primarily due to a decrease in restricted cash of \$40.6 and \$67.2 million in 2013 and 2012, respectively.

*Capital assets, net* increased \$184.2 million or 5.8% and \$142.2 million or 4.7% in 2013 and 2012, respectively. The increase is due primarily to capital improvements that are required to maintain and rehabilitate aging infrastructure in order to provide safe and reliable services to customers, to prepare for future demand and to meet environmental and regulatory requirements.



## **COLORADO SPRINGS UTILITIES**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS** As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### ***Deferred Outflows of Resources***

*Deferred outflows of resources* decreased \$221.7 million in 2013 due to a decrease of \$226.4 million in unrealized loss on deferred cash flow hedge derivatives and an increase of \$4.7 million in loss on debt refundings. An increase of \$40.6 million in 2012 is primarily due to the implementation of GASB Statement No. 65 *Items Previously Reported as Assets and Liabilities* ("GASB 65") in the amount of \$26.1 million for the loss on debt refundings. In addition, \$14.5 million is attributed to unrealized loss on deferred cash flow hedge derivatives.

#### ***Liabilities***

*Current liabilities* increased \$3.5 million in 2013 primarily due to increases of \$6.0 million in accounts payable, \$5.0 million in current maturities of restricted bonds and \$4.0 million in other liabilities. These increases were partially offset by a decrease in derivative instruments of \$12.1 million. A decrease of \$33.7 million in 2012 is primarily due to decreases of \$39.0 million in derivative instruments, \$3.0 million in other liabilities and \$1.5 million in restricted accrued interest. These decreases were partially offset by increases of \$5.6 million in current maturities of restricted bonds, \$2.7 million in accounts payable and \$1.0 million in unrestricted accrued salaries and benefits.

*Noncurrent liabilities* decreased \$4.2 million in 2013 primarily due to a decrease of \$85.7 million in derivative instruments and \$2.0 million in customer advances for construction. These decreases were partially offset by an increase of \$83.8 million in revenue bonds, net of unamortized premiums and discounts. Revenue bonds, net of unamortized premiums and discounts comprises the majority of the noncurrent liabilities with a balance of \$2.3 billion.

*Noncurrent liabilities* increased \$66.3 million in 2012 primarily due to an increase of \$75.6 million in revenue bonds, net of unamortized premiums and discounts. \$26.1 million of the increase relates to the loss on debt refundings being reclassified to deferred outflows of resources due to the implementation of GASB 65. The increase was partially offset by decreases of \$8.7 million in derivative instruments and \$1.5 million in notes and loans payable. Revenue bonds, net of unamortized premiums and discounts comprises the majority of the noncurrent liabilities with a balance of \$2.3 billion.

#### ***Deferred Inflows of Resources***

*Deferred inflows of resources* decreased \$60.8 million in 2013 due to a decrease of \$60.6 million in unrealized gains on deferred gains on deferred cash flow hedge derivatives. An increase of \$58.2 million in 2012 is primarily due to the implementation of GASB 65 in the amount of \$55.7 million in unrealized gains on deferred cash flow hedge derivatives.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### **CONDENSED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION**

	2013	2012	2011*
	(in thousands)		
Operating Revenues	\$ 823,760	\$ 849,746	\$ 830,522
Operating Expenses	(667,268)	(674,480)	(741,607)
Operating Income	156,492	175,266	88,915
Nonoperating Expenses	(135,680)	(72,252)	(73,097)
Income Before Contributions, Transfers and Extraordinary Items	20,812	103,014	15,818
Capital contributions	44,490	47,143	33,635
Transfers - surplus payments to the City	(31,845)	(30,595)	(31,585)
Transfers - other	(308)	(640)	(78)
Extraordinary expense	(507)	-	-
Change in Net Position	32,642	118,922	17,790
Total Net Position, January 1	1,453,356	1,334,434	1,316,644
Total Net Position, December 31	\$ 1,485,998	\$ 1,453,356	\$ 1,334,434

\* 2011 data was not adjusted for GASB Statement No. 65 conformance.

#### **Operating Revenues**

Operating Revenues in 2013 decreased \$26.0 million or 3.1% from 2012 driven primarily by decreases in water and wastewater revenue of \$30.2 million and \$1.3 million, respectively, offset partially by increases in electric and natural gas revenues of \$10.5 million and \$1.1 million, respectively. Operating revenue changes are driven by base rate changes and unit sales that are primarily affected by weather.

Operating Revenues in 2012 increased \$19.2 million or 2.3% from 2011 driven primarily by increases in electric and water revenue of \$9.4 million and \$27.3 million, respectively, offset partially by decreases in natural gas and wastewater revenues of \$15.5 million and \$1.6 million, respectively. Operating revenue changes are driven by base rate changes and unit sales that are primarily affected by weather.

#### **Operating Expenses**

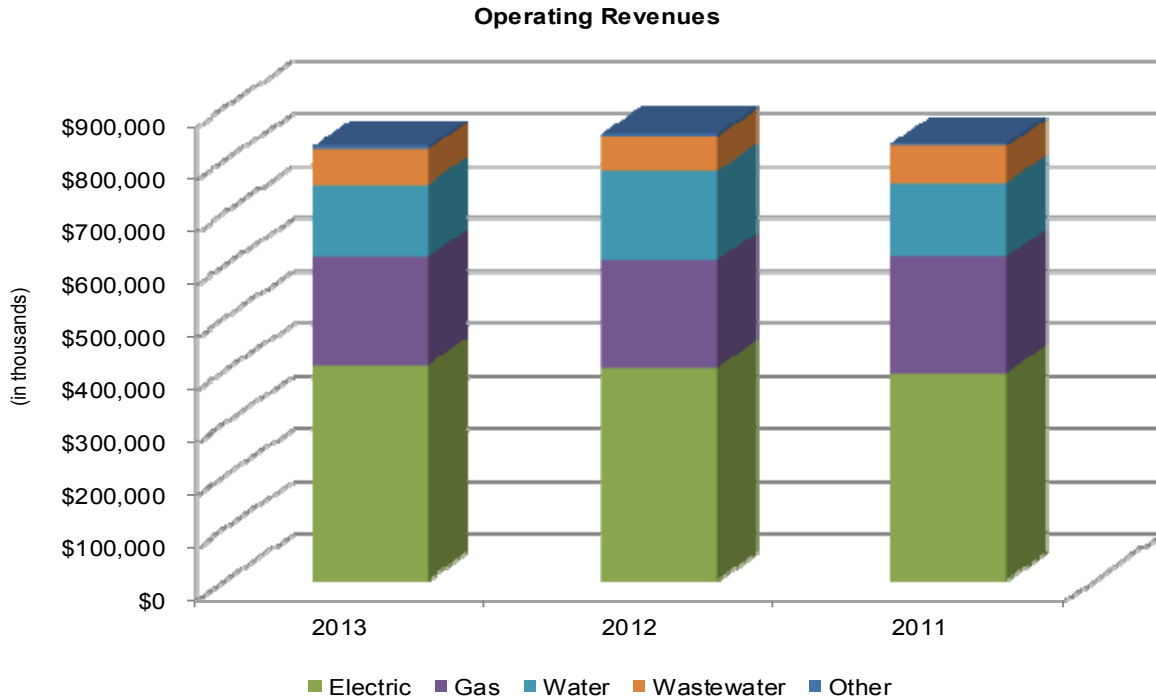
Operating Expenses in 2013 decreased \$7.2 million or 1.1% from 2012 primarily due to decreased commodity prices for natural gas and fuels used in electric generation.

Operating Expenses in 2012 decreased \$67.1 million or 9.1% from 2011 primarily due to decreased commodity prices for natural gas and fuels used in electric generation.

## COLORADO SPRINGS UTILITIES

MANAGEMENT'S DISCUSSION AND ANALYSIS  
As of and for the Years Ended December 31, 2013, 2012 and 2011  
(Unaudited)

### CHANGES IN OPERATING REVENUES AND EXPENSES



#### Operating Revenues 2013 to 2012:

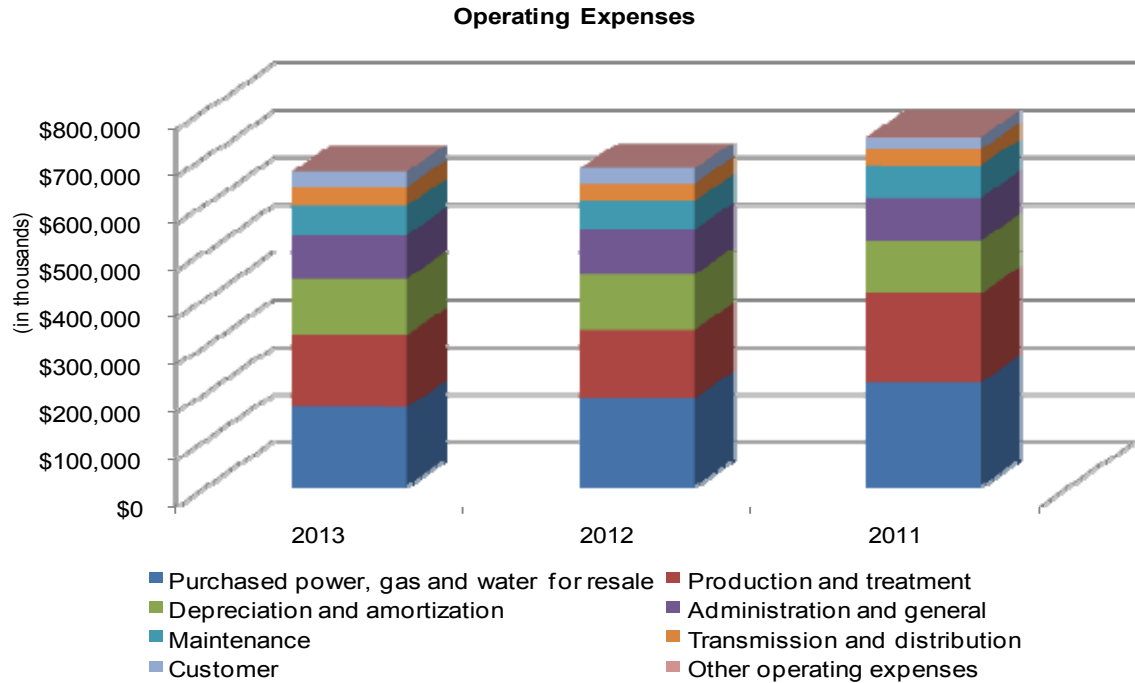
- \$4.1 million - Electric
  - Non-Fuel base rates increased an overall 4.5%
- (\$30.2) million - Water
  - Overall system unit sales decreased approximately 27.0% due to drought restrictions implemented in May 2013 and unusually wet weather during the late irrigation season

#### Operating Revenues 2012 to 2011:

- \$9.4 million - Electric
  - Overall system unit sales increased approximately 1.0%
  - Non-Fuel base rates increased an overall 5.0%
- (\$15.5) million - Gas
  - Overall system unit sales decreased approximately 13.5% primarily due to warmer than normal weather during the heating season
  - Non-Fuel base rates increased an overall 1.9%
- \$27.3 million - Water
  - Overall system unit sales excluding unit adjustments increased approximately 6.0% due to hot and dry weather during the irrigation season
  - Non-Fuel base rates increased an overall 10.0%

## COLORADO SPRINGS UTILITIES

MANAGEMENT'S DISCUSSION AND ANALYSIS  
As of and for the Years Ended December 31, 2013, 2012 and 2011  
(Unaudited)



### Operating Expenses 2013 to 2012:

- (\$13.6) million - Decreased commodity prices for natural gas and fuels used in electric generation
- \$4.1 million - Labor and benefits expenses driven by employee pay changes, increasing benefits costs and work shifting between capital and operations
- \$2.2 million - Depreciation of assets

### Operating Expenses 2012 to 2011:

- (\$85.1) million - Decreased commodity prices for natural gas and fuels used in electric generation
- \$9.6 million - Labor and benefits expenses driven by employee pay changes, increasing benefits costs and work shifting between capital and operations
- \$4.6 million - Depreciation of assets

## **COLORADO SPRINGS UTILITIES**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS** As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### **CASH AND LIQUIDITY**

Current assets include unrestricted cash deposits in banks and unrestricted investments in U.S. Treasury Notes and U.S. Government Agency Securities. The total of these two unrestricted cash sources was \$225.8 million at December 31, 2013, an increase of \$48.0 million, or 27.0%, from 2012 due primarily to the return of collateral related to interest rate hedge agreements held by financial counterparties. The total of unrestricted cash sources was \$177.8 million at December 31, 2012, an increase of \$80.6 million, or 82.8%, from 2011. Two interest rate swap agreements were novated resulting in the return of cash collateral held by financial counterparties in the amount of \$39.3 million. In addition, capital spending was deferred to future periods and additional unrestricted cash was generated from higher utility rates.

Current and noncurrent assets include restricted cash deposits in banks and investments in repurchase agreements. The total of these two restricted funding sources was \$214.6 million at December 31, 2013, a decrease of \$36.2 million, or 14.4%, from 2012. The total of restricted funding sources was \$250.8 million at December 31, 2012, a decrease of \$56.7 million, or 18.4%, from 2011. The decline in both years was due to the return of collateral related to interest rate hedge agreements. Collateral returned is reclassified from restricted to unrestricted cash. In addition, capital project funds decreased \$42.1 million, or 24.2%. There was not a need to issue bonds in 2011 to finance capital projects in 2012.

A source of unrestricted liquidity that is not reflected on the balance sheet is revolving lines of credit. Utilities has had one or more lines of credit in place since 2002. Although never drawn, the lines are maintained to ensure liquidity is available, if needed, through major unforeseen natural disasters when the ability to collect revenue could be impaired, for working capital during an unplanned or extended plant outage or as a collateral posting source with financial counterparties on hedging agreements. In September 2013, Utilities established \$75.0 million in lines of credit with two banks: KeyBank National Association ("KeyBank") for \$50.0 million and U.S. Bank National Association ("U.S. Bank") for \$25.0 million, both with three year terms. The total available lines of credit remained at \$75.0 million at December 31, 2013.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

Summary of the days cash on hand as of December 31:

	<u>2013</u>	<u>2012</u> (in thousands)	<u>2011</u>
Cash, cash equivalents and investments - unrestricted	<u>\$ 225,818</u>	<u>\$ 177,857</u>	<u>\$ 97,303</u>
Cash Expense per Day			
Total Operating Expenses	\$ 667,268	\$ 674,480	\$ 741,607
Less: Depreciation and amortization	(118,430)	(116,185)	(111,552)
Project Write-off	-	-	(27,342)
Net Cash Expense	<u>\$ 548,838</u>	<u>\$ 558,295</u>	<u>\$ 602,713</u>
Number of Days in a Period	<u>365</u>	<u>366</u>	<u>365</u>
Net Cash Expense Per Day	<u>\$ 1,504</u>	<u>\$ 1,525</u>	<u>\$ 1,651</u>
Days of Cash on hand	<u>150.2</u>	<u>116.6</u>	<u>58.9</u>

Note: Immaterial differences may occur due to rounding.

### CAPITAL ASSETS AND TOTAL LONG-TERM DEBT

Capital assets and total long-term debt with comparative information as of December 31:

#### CAPITAL ASSETS

	<u>2013</u>	<u>2012</u> (in thousands)	<u>2011</u>
Plant in service	\$ 4,621,456	\$ 4,514,735	\$ 4,389,582
Construction work in progress	648,178	460,110	335,831
Accumulated depreciation and amortization	<u>(1,881,433)</u>	<u>(1,770,809)</u>	<u>(1,663,620)</u>
Total Capital Assets (net of Accumulated Depreciation and Amortization)	<u>\$ 3,388,201</u>	<u>\$ 3,204,036</u>	<u>\$ 3,061,793</u>

Note: Immaterial differences may occur due to rounding.

Utilities' capital expenditures for the years ended December 31, 2013, 2012 and 2011, were \$290.5 million, \$246.4 million, and \$203.3 million, respectively. Electric capital expenditures included emissions control technology as well as general system improvements. Water capital expenditures included construction of the Southern Delivery System ("SDS") to ensure the community has an adequate water supply into the future as well as general system improvements. Capital expenditures on facilities included technology additions and enhancements to the telecommunication, computing and applications infrastructure. The following capital expenditure table reflects the capital expenditures by system.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### ***CAPITAL EXPENDITURES BY SYSTEM***

Capital expenditures by system as of December 31:

	<u>2013</u>	<u>2012</u> (in thousands)	<u>2011</u>
Electric			
Emissions Controls	\$ 30,674	\$ 32,965	\$ (14,968)
General System Improvements	56,609	51,690	65,477
Total Electric	<u>87,283</u>	<u>84,655</u>	<u>50,509</u>
Water			
Southern Delivery System	135,800	99,872	78,915
General System Improvements	36,772	28,671	32,154
Total Water	<u>172,572</u>	<u>128,543</u>	<u>111,069</u>
Natural Gas	11,725	13,274	12,156
Wastewater	10,612	9,903	14,722
Facilities and Information Technology	8,346	10,016	14,811
Total Capital Expenditures	<u>\$ 290,538</u>	<u>\$ 246,391</u>	<u>\$ 203,267</u>

Note: Immaterial differences may occur due to rounding.

#### ***TOTAL LONG-TERM DEBT***

	<u>2013</u>	<u>2012</u> (in thousands)	<u>2011*</u>
Tax-exempt revenue bonds	\$ 1,819,160	\$ 1,736,104	\$ 1,699,479
Taxable revenue bonds	492,480	498,170	503,730
Loans	18,167	19,678	21,089
Total Long-Term Debt	<u>\$ 2,329,807</u>	<u>\$ 2,253,952</u>	<u>\$ 2,224,298</u>

\* 2011 data was not adjusted for GASB Statement No. 65 conformance.

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

Debt Ratio as of December 31:

	2013	2012	2011*
		(in thousands)	
Current Maturities of Bonds-Restricted	\$ 55,764	\$ 50,774	\$ 45,149
Current Maturity of Notes and Loans Payable-Restricted	1,531	1,511	1,412
Long-Term Revenue Bonds, Net	2,345,644	2,261,876	2,207,635
Long-Term Notes and Loans Payable	16,636	18,167	19,678
Net Gain/Loss on Refundings	(28,423)	(23,538)	(21,386)
Total	<u>2,391,152</u>	<u>2,308,790</u>	<u>2,252,488</u>
Net Position	<u>\$ 1,485,998</u>	<u>\$ 1,453,356</u>	<u>\$ 1,334,434</u>
Debt Ratio	<u>61.7%</u>	<u>61.4%</u>	<u>62.8%</u>

\* 2011 data was not adjusted for GASB Statement No. 65 conformance.

Note: Immaterial differences may occur due to rounding.

Utilities engages Moody's Investor Services ("Moody's"), Standard & Poor's ("S&P") and Fitch Ratings ("Fitch") to provide credit rating services. Utilities' long-term credit ratings are as follows:

	2013		2012		2011	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Moody's	Aa2	Stable	Aa2	Stable	Aa2	Negative
S&P	AA	Stable	AA	Stable	AA	Stable
Fitch	AA	Stable	AA	Stable	AA	Stable

Utilities' short-term ratings on variable rate bonds are as follows:

Bond Issue	2013	2012	2011
2000A	VMIG1 / NR / NR	VMIG1 / NR / NR	VMIG1 / NR / NR
2002C	VMIG1 / A-1+ / NR	VMIG1 / A-1 / NR	VMIG1 / A-1 / NR
2004A	VMIG1 / A-1 / F1	VMIG2 / A-1 / F1	VMIG1 / A-1 / F1
2005A	VMIG1 / A-1 / F1+	VMIG1 / A-1 / F1+	VMIG1 / A-1 / F1
2006A	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1+
2006B	VMIG2 / NR / F1+	VMIG2 / NR / F1+	VMIG2 / NR / F1+
2007A	VMIG1 / A-1+ / F1+	VMIG1 / A-1+ / F1+	VMIG1 / A-1+ / F1+
2007B	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1
2008A	VMIG1 / A-1 / F1	VMIG2 / A-1 / F1	VMIG1 / A-1 / F1
2009C	VMIG1 / A-1+ / F1+	VMIG1 / A-1+ / F1+	VMIG1 / A-1+ / F1+
2010C	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1	VMIG1 / A-1 / F1+
2012A	VMIG1 / A-1+ / F1+	VMIG1 / A-1+ / F1+	N/A



## **COLORADO SPRINGS UTILITIES**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS** As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

Utilities' short-term ratings are based on the credit ratings of banks providing liquidity support for the variable rate bonds. Short-term credit rating assignments are by Moody's, S&P and Fitch, respectively. "NR" indicates a bond issue is not rated by one or more credit rating agency. "N/A" indicates a bond issue did not exist when credit ratings were assigned.

#### ***FINANCING***

Utilities conducts its financing activities based on strategies and guidance provided by the long-term Plan of Finance ("Plan"). Fundamental to the Plan are goals and objectives that Utilities has developed and targeted as important measures for future performance. These include the following:

- Maintenance of long-term credit ratings of Aa2/AA/AA by Moody's, S&P and Fitch, respectively
- A focus on targeted financial metrics: Debt Ratio, Days Cash on Hand and Adjusted Debt Service Coverage
- The minimization of rate impacts resulting from financing activities in each utility service (Electric, Gas, Water and Wastewater)

The Plan development process includes analyzing funding options, measuring risk/benefits of the options, setting parameters for optimal structures such as fixed versus floating rate debt, term of debt and other and reviewing key ratios of peers. The Plan process incorporates Utilities' Financial Risk Management Policy and a review of the legal framework to enable successful implementation of potential financing alternatives. The following briefly describes the major financing transactions Utilities executed in 2013, all of which were in direct support of the Plan:

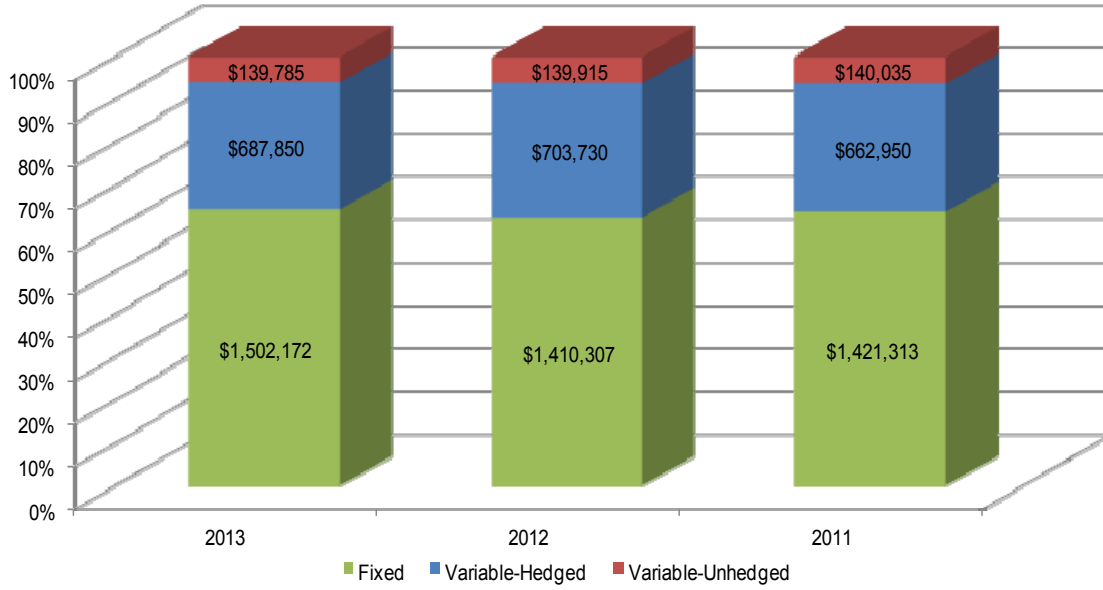
- In April 2013, Utilities issued the 2013A refunding bonds to achieve debt service savings on existing debt. Overall, \$11.2 million in total savings will be realized on a gross basis over the life of the bonds with present value savings of 9.2% or \$9.0 million. The True Interest Cost ("TIC") that Utilities will realize is 3.5%.
- In September 2013, Utilities issued the 2013B fixed rate 30-year bonds to fund a portion of the SDS project and a portion of general system capital improvements. The total project fund for this bond issue was \$130.0 million. The TIC that Utilities will realize is 4.5%.
- In September 2013, Utilities entered into Line of Credit agreements with KeyBank for \$50.0 million and U.S. Bank for \$25.0 million, both with three year terms. Credit rating agencies view the multi-year terms of undrawn Lines of Credit as an important rating factor when evaluating liquidity positions. Also achieved was more diversity by entering into agreements with two providers rather than one.
- In August 2013, Utilities renewed standby bond purchase agreements for 2006A, 2007A and 2010C bond issues, supporting \$179.0 million in variable rate debt. The existing agreements with JP Morgan (2006A, 2007A) and Wells Fargo (2010C) did not require significant amendments. In addition, Utilities negotiated reduced pricing on each agreement.

# COLORADO SPRINGS UTILITIES

MANAGEMENT'S DISCUSSION AND ANALYSIS  
As of and for the Years Ended December 31, 2013, 2012 and 2011  
(Unaudited)

The following chart illustrates the variable and fixed financing structure for the years ended December 31:

**Variable vs. Fixed Rate Debt**  
(in thousands)

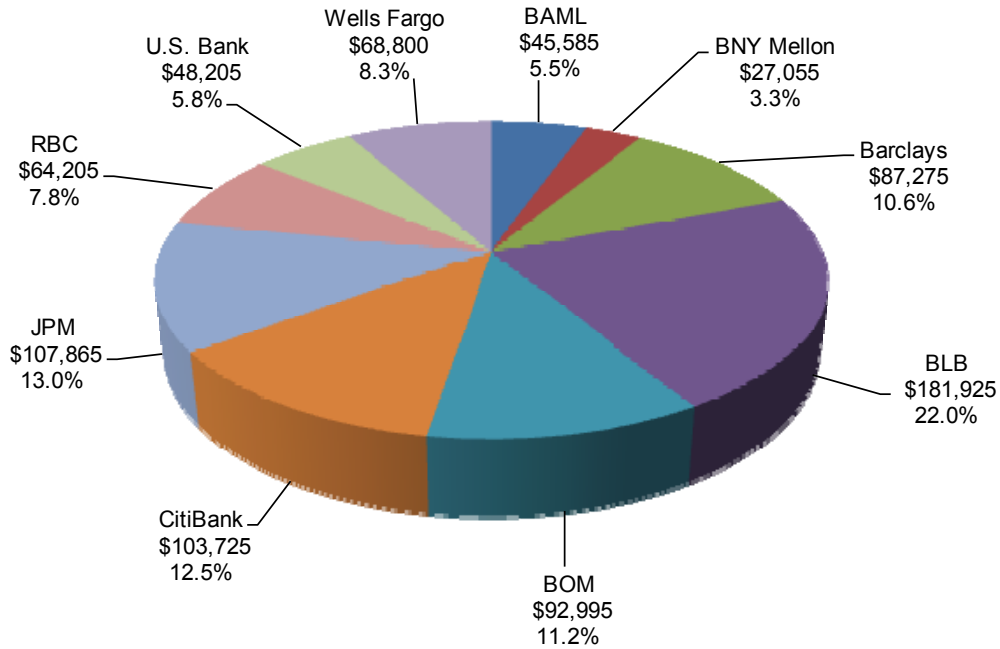


## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

The following chart illustrates the variable rate liquidity providers as of December 31, 2013:

**Variable Rate Debt - Liquidity Providers**  
(in thousands)



### **DEBT SERVICE COVERAGE**

Summary of the debt service coverage for years ended December 31:

	2013	2012	2011
		(in thousands)	
Operating Revenues	\$ 823,760	\$ 849,747	\$ 830,522
Operating Expenses	(667,268)	(674,480)	(741,606)
Project Write-off	-	-	27,342
Depreciation and amortization	118,430	116,185	111,552
Operating Revenues Available for Debt Service	274,922	291,452	227,810
Interest earnings (excl. interest on bonds)	8,431	11,006	11,570
Development fees	30,766	35,343	29,696
Net Pledged Revenues	<u>\$ 314,119</u>	<u>\$ 337,801</u>	<u>\$ 269,076</u>
Fiscal Year Debt Service	<u>\$ 154,193</u>	<u>\$ 151,142</u>	<u>\$ 132,956</u>
Debt Service Coverage Ratio	<u>2.04</u>	<u>2.23</u>	<u>2.02</u>

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### RESTRICTED ASSETS

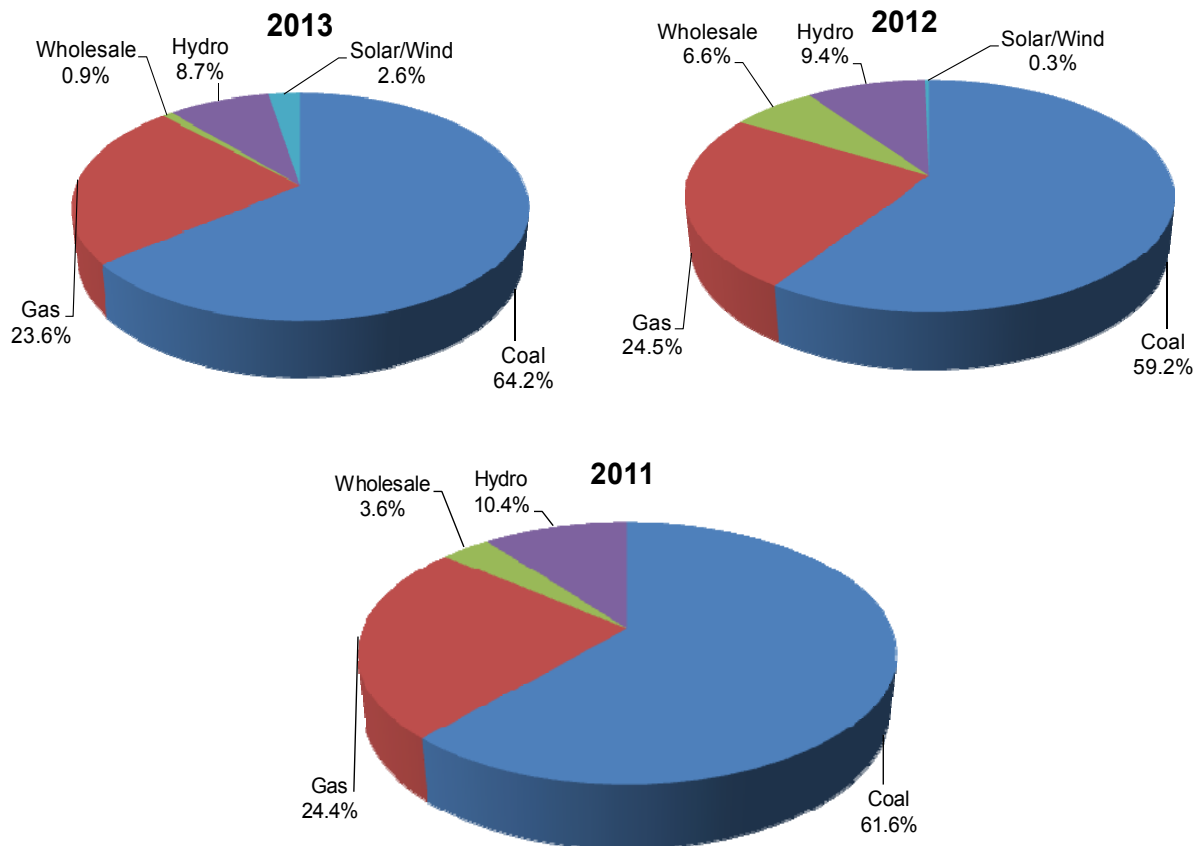
Debt proceeds available for the acquisition, construction or improvement of capital assets that are unspent at year end are classified as restricted noncurrent assets.

Utilities' Bond Ordinances require individual reserve funds by bond issue, but allow Utilities to use surety bonds in lieu of cash bond reserve funds. The Bond Ordinances require that monies be restricted in separate accounts for the retirement of principal and payment of interest.

Under terms of International Swaps and Derivatives Association ("ISDA"), agreements covering interest rate and energy hedge positions held between Utilities and various counterparties, secured parties, are entitled to hold posted collateral directly or through a custodian. The value or amount of collateral posted is subject to thresholds and counterparty credit ratings established in the ISDA. Cash collateral held directly by Utilities is classified as a restricted noncurrent asset. The corresponding liability is classified as noncurrent on the Statements of Net Position.

#### SOURCES OF GENERATION

The following illustrates Utilities' sources of generation for the years ended December 31:



## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

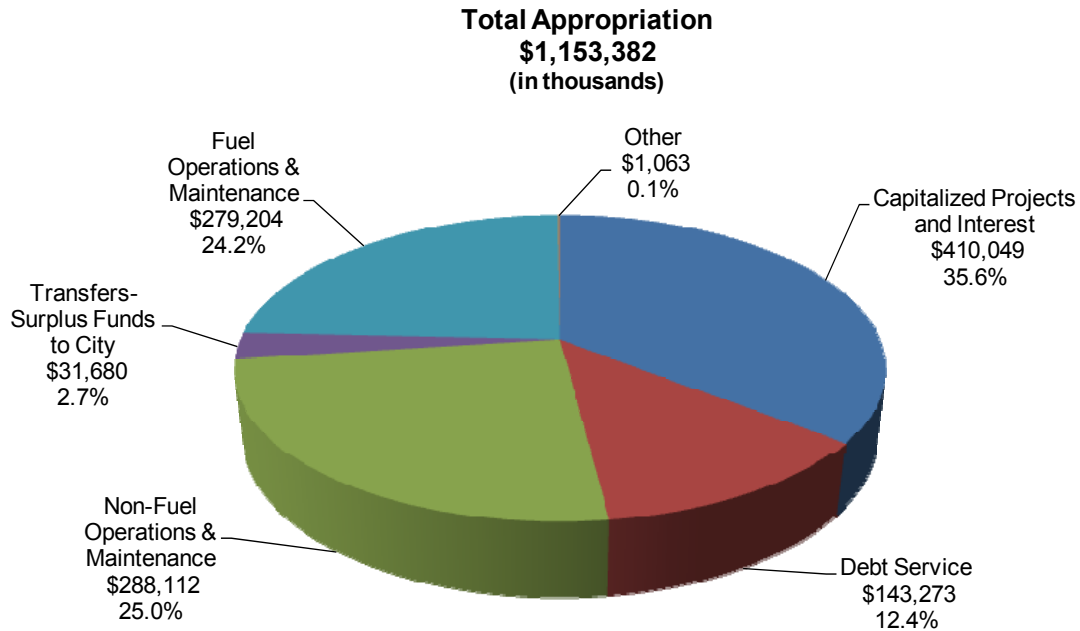
#### PEAK DEMAND

	Peak Demand	Peak Day
Electric - maximum hourly peak demand (Megawatt)	904	Jun 26, 2012
Natural Gas - maximum daily peak demand (Million Cubic Feet)	266,786	Feb 01, 2011
Water - maximum daily pumpage (Millions of Gallons)	182,405	Jul 07, 2001

#### BUDGETARY HIGHLIGHTS FOR 2014

The following information contains statements that to the extent they are not recitations of historical fact, constitute "forward-looking statements." A number of important factors affecting Utilities' business and financial results could cause actual results to differ materially from those stated in the forward-looking statements. Utilities does not plan to issue updates or revisions to forward-looking statements contained in this MD&A.

#### APPROPRIATIONS SUMMARY



## COLORADO SPRINGS UTILITIES

### MANAGEMENT'S DISCUSSION AND ANALYSIS As of and for the Years Ended December 31, 2013, 2012 and 2011 (Unaudited)

#### ***CAPITALIZED PROJECTS AND INTEREST***

	2014 Approved Budget
	(in thousands)
Electric	\$ 112,871
Streetlight	927
Natural Gas	17,133
Water	233,268
Wastewater	11,586
Common	15,206
Total before AFUDC* and Capitalized Interest	<u>390,991</u>
AFUDC and Capitalized Interest	19,058
Total	<u><u>\$ 410,049</u></u>

\*Allowance for Funds Used During Construction ("AFUDC")

Capital improvements are required to maintain and rehabilitate aging infrastructure in order to provide safe and reliable services to customers, to prepare for future demand and to meet environmental and regulatory requirements.

#### **CONTACTING UTILITIES' FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, customers, investors, creditors and other financial users with a general overview of Utilities' finances. If you have questions about this report or need additional financial information, contact the Chief Planning and Finance Officer, Colorado Springs Utilities, P.O. Box 1103, Mail Code 950, Colorado Springs, CO. 80947-0950.

## COLORADO SPRINGS UTILITIES

### STATEMENTS OF NET POSITION December 31, 2013 and 2012

	2013	2012
	(in thousands)	
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents - unrestricted	\$ 111,039	\$ 111,679
Cash and cash equivalents - restricted	32,038	27,576
Investments - unrestricted	114,779	66,178
Accounts receivable, net - unrestricted	102,292	105,752
Accounts receivable, net - restricted	2,198	2,239
Due from other City funds	6,975	3,723
Interest receivable	140	100
Inventories	49,612	48,434
Prepaid expenses	8,844	13,772
Derivative instruments	-	31
Other current assets	21	-
	<b>427,938</b>	<b>379,484</b>
<b>Noncurrent Assets</b>		
Cash and cash equivalents - restricted	181,126	221,713
Investments - restricted	1,431	1,483
Investment in joint ventures	1,198	1,275
Other (including utility acquisition adjustment)	116,066	115,236
Capital assets:		
Plant in service	4,621,456	4,514,735
Construction work in progress	648,178	460,110
Accumulated depreciation and amortization	(1,881,433)	(1,770,809)
Total Capital Assets (net of accumulated depreciation and amortization)	3,388,201	3,204,036
<b>Total Noncurrent Assets</b>	<b>3,688,022</b>	<b>3,543,743</b>
<b>Total Assets</b>	<b>4,115,960</b>	<b>3,923,227</b>
<b>Deferred Outflows of Resources</b>		
Deferred cash flow hedges - unrealized loss on derivatives	47,237	273,619
Loss on debt refundings	30,798	26,100
<b>Total Deferred Outflows of Resources</b>	<b>78,035</b>	<b>299,719</b>
<b>Total Assets and Deferred Outflows of Resources</b>	<b>\$ 4,193,995</b>	<b>\$ 4,222,946</b>

The accompanying notes are an integral part of these statements.

## COLORADO SPRINGS UTILITIES

### STATEMENTS OF NET POSITION - continued December 31, 2013 and 2012

	2013	2012
	(in thousands)	
<b>Liabilities</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 84,082	\$ 78,099
Due to other City funds	4,152	4,133
Current maturities of bonds - restricted	55,764	50,774
Current portion of notes and loans payable - restricted	1,531	1,511
Accrued interest - restricted	12,572	12,189
Accrued salaries and benefits - unrestricted	5,645	4,564
Accrued salaries and benefits - restricted	2,776	3,360
Compensated absences	7,536	7,474
Claims and judgments	15	356
Derivative instruments	194	12,326
Other	8,390	4,389
	<b>182,657</b>	<b>179,175</b>
<b>Noncurrent Liabilities</b>		
Customer deposits	2,174	2,095
Notes and loans payable	16,636	18,167
Compensated absences	5,754	5,564
Customer advances for construction	8,508	10,475
Revenue bonds, net of unamortized premiums and discounts	2,345,644	2,261,876
Municipal solid waste landfill closure and postclosure care	4,107	3,969
Derivative instruments	137,485	223,186
Other	2,657	1,876
	<b>2,522,965</b>	<b>2,527,208</b>
	<b>2,705,622</b>	<b>2,706,383</b>
<b>Deferred Inflows of Resources</b>		
Deferred cash flow hedges - unrealized gains on derivatives	-	60,645
Gain on debt refundings	2,375	2,562
	<b>2,375</b>	<b>63,207</b>
<b>Net Position</b>		
Net investment in capital assets	1,173,004	1,067,642
Restricted		
Collateral	6,601	50,801
Debt service	13,582	12,149
Health care benefits	3,535	3,026
Other purposes	4,548	2,451
Unrestricted	284,728	317,287
	<b>1,485,998</b>	<b>1,453,356</b>
	<b>1,485,998</b>	<b>1,453,356</b>
	<b>\$ 4,193,995</b>	<b>\$ 4,222,946</b>

The accompanying notes are an integral part of these statements.



## COLORADO SPRINGS UTILITIES

### STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION Years ended December 31, 2013 and 2012

	2013	2012
	(in thousands)	
<b>Operating Revenues</b>		
Electric	\$ 407,397	\$ 403,326
Streetlight	4,250	3,921
Gas	206,182	205,060
Water	138,981	169,152
Wastewater	64,762	66,092
Products and services	2,188	2,195
	<b>823,760</b>	<b>849,746</b>
<b>Operating Expenses</b>		
Production and treatment	153,635	144,361
Purchased power, gas and water for resale	168,003	188,627
Transmission and distribution	39,343	36,386
Maintenance	63,023	61,793
Administration and general	93,143	96,185
Customer service and information	11,027	10,309
Customer accounting and collection	20,362	20,284
Products and services	12	62
Franchise taxes	290	288
Depreciation and amortization	118,430	116,185
	<b>667,268</b>	<b>674,480</b>
<b>Operating Income</b>	<b>156,492</b>	<b>175,266</b>
<b>Nonoperating Revenues (Expenses)</b>		
Derivative instruments gain/(loss)	(67,936)	6,177
Investment income	2,322	2,689
Other revenues	16,679	13,053
Other expenses	(5,276)	(5,299)
Interest expense	(81,469)	(88,872)
	<b>(135,680)</b>	<b>(72,252)</b>
<b>Income Before Contributions, Transfers and Extraordinary Items</b>	<b>20,812</b>	<b>103,014</b>
Capital contributions	44,490	47,143
Transfers - surplus payments to the City	(31,845)	(30,595)
Transfers - other	(308)	(640)
Extraordinary expense	(507)	-
	<b>32,642</b>	<b>118,922</b>
<b>Change in Net Position</b>	<b>32,642</b>	<b>118,922</b>
<b>Total Net Position, January 1</b>	<b>1,453,356</b>	<b>1,334,434</b>
<b>Total Net Position, December 31</b>	<b>\$ 1,485,998</b>	<b>\$ 1,453,356</b>

The accompanying notes are an integral part of these statements.

## COLORADO SPRINGS UTILITIES

### STATEMENTS OF CASH FLOWS Years ended December 31, 2013 and 2012

	2013	2012
	(in thousands)	
<b>Cash Flows From Operating Activities</b>		
Receipts from customers and users	\$ 812,275	\$ 834,559
Receipts from interfund activities	13,724	18,802
Other cash receipts, net	6,816	5,339
Payments to suppliers	(399,466)	(407,687)
Payments to/on behalf of employees	(170,955)	(170,917)
Payments for interfund activities	(10,132)	(10,041)
	<b>252,262</b>	<b>270,055</b>
<b>Cash Flows from Noncapital Financing Activities</b>		
Other receipts/(payments), net	(308)	(665)
Surplus payments to the City	(31,568)	(30,773)
Receipts from federal/state grants	292	335
	<b>(31,584)</b>	<b>(31,103)</b>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Proceeds from issuance of revenue bonds	225,140	315,685
Bond issuance and other related costs	8,206	26,289
Capital expenditures	(237,442)	(212,178)
Capital contributions	33,814	32,466
Repayment and refunding of long-term debt	(149,285)	(286,031)
Interest payments on long-term debt	(101,901)	(104,440)
Interest payments - other	(15)	(7)
Proceeds from sale of assets	1,506	1,994
Receipts from federal/state grants	8,815	8,551
	<b>(211,162)</b>	<b>(217,671)</b>
<b>Cash Flows from Investing Activities</b>		
Interest received on investments	2,329	2,703
Distributions from joint ventures	193	-
Purchases of investments	(62,803)	(51,120)
Proceeds from sales and maturities of investments	14,000	27,000
	<b>(46,281)</b>	<b>(21,417)</b>
<b>Decrease in Cash and Cash Equivalents</b>	(36,765)	(136)
<b>Cash and Cash Equivalents, January 1</b>	360,968	361,104
<b>Cash and Cash Equivalents, December 31</b>	<b>\$ 324,203</b>	<b>\$ 360,968</b>

The accompanying notes are an integral part of these statements.

## COLORADO SPRINGS UTILITIES

### STATEMENTS OF CASH FLOWS - continued Years ended December 31, 2013 and 2012

	2013	2012
	(in thousands)	
<b>Reconciliation of operating income to net cash provided by (used in) operating activities</b>		
Operating Income	\$ 156,492	\$ 175,266
Adjustments to Operating Income:		
Depreciation and amortization	118,430	116,185
Other	(29,400)	(18,726)
<b>(Increase) Decrease in Assets</b>		
Accounts receivable	(211)	1,252
Inventories	(1,179)	6,004
Prepaid expenses	4,928	(6,111)
Other assets	(2,201)	(7,258)
<b>Increase (Decrease) in Liabilities</b>		
Accounts payable	4,355	2,369
Accrued salaries, vacation and sick leave benefits	748	2,122
Other liabilities	300	(1,048)
<b>Net Cash Provided by Operating Activities</b>	<b>\$ 252,262</b>	<b>\$ 270,055</b>
<b>Noncash Investing, Capital and Related Financing Activities</b>		
Investment derivatives	\$ (67,936)	\$ 6,177
Noncash acquisition of plant in service		
(incurrence of payable)	27,412	27,567
Noncash capital contributions	13,723	11,799
Noncash repayment of long-term debt	10,111	9,271
Amortization of loss on refunding	1,553	1,362
Amortization and charge-off of debt discount	87	112

The accompanying notes are an integral part of these statements.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### **NOTE 1 - FINANCIAL REPORTING ENTITY**

Utilities is an Enterprise Fund of the City of Colorado Springs, Colorado ("City"). The financial statements present only entities for which Utilities is considered to be financially accountable. The Chief Executive Officer ("CEO") of Utilities directs and manages Utilities. The CEO reports to and is appointed by the City Council. Major policy decisions are subject to the approval of the Board of Directors of Utilities ("Utilities Board"), which also sits as the City Council. The financial statements do not purport to, and do not present the financial position of the City, component units, or its joint venture as of December 31, 2013 and 2012, nor the changes in its financial position and its cash flows, where applicable, for the years then ended.

Utilities operates an electric generation, transmission and distribution system; a streetlight system; a natural gas distribution system; a water collection, treatment and distribution system; and a wastewater collection and treatment system. Utilities' service area includes the City, Manitou Springs and many of the suburban residential areas surrounding the City. The military installations of Fort Carson Army Base, Peterson Air Force Base, Cheyenne Mountain Air Force Station and the United States Air Force Academy receive electric service, natural gas supply and transportation service and water service from Utilities, and Peterson Air Force Base also receives wastewater treatment service.

The activity of component units is reported in the City's financial statements due to the extent of their operational and financial relationship. City component units are discussed further in the Notes to Financial Statements ("Notes"). Separate financial statements of these component units can be obtained from the Chief Planning and Finance Officer, Colorado Springs Utilities, P.O. Box 1103, Mail Code 950, Colorado Springs, CO 80947-0950.

Joint ventures are legal entities or other organizations that result from contractual arrangements and are owned, operated or governed by two or more participants as separate and specific activities subject to joint control, in which the participants retain an ongoing financial interest or an ongoing financial responsibility. The joint venture in which Utilities participates is further discussed in the Notes.

#### **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### ***BASIS OF ACCOUNTING***

Utilities' accounting records are maintained and the accompanying financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") as applied to units of local government and promulgated by the Governmental Accounting Standards Board ("GASB"). Consolidated financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

##### ***RECENT ACCOUNTING PRONOUNCEMENTS***

##### ***GASB Pronouncement Implementation in 2013***

GASB Statement No. 65 *Items Previously Reported as Assets and Liabilities* ("GASB 65") was issued in March 2012 effective for periods beginning after December 15, 2012. The objective of GASB 65 is to establish accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. Additionally, GASB 65 requires that debt issuance costs be recognized as expense in the period incurred, except where accounting and financial reporting for regulated operations may provide reasonable assurance of the existence of a regulatory asset pursuant to GASB Statement

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* (incorporating Accounting Standards Codification 980 ("ASC 980") and Statement of Financial Accounting Standards 71 - Accounting for the Effects of Certain Types of Regulation). ASC 980 is the accounting guidance used by public utilities to recover costs through rates charged to their ratepayers, make their operating benchmarks comparable to their investor-owned peer utilities and also match their accounting to utility industry standards. The adoption of GASB 65 resulted in the reclassification of gains and losses on debt refundings previously reported as assets or liabilities to deferred inflows or deferred outflows of resources. On March 26, 2013, City Council approved Resolution 26-13 establishing a regulatory asset for expenditures associated with debt issuance costs effective as of January 1, 2013 to be amortized over the life of the related debt. The prior year has been adjusted for this change. Refer to Note 18 for additional information.

#### ***GASB Pronouncement Implementations in 2012***

GASB Statement No. 64 *Derivative Instruments: Application of Hedge Accounting Termination Provisions, An Amendment of GASB Statement No. 53* ("GASB 64") was issued in June 2011 effective for periods beginning after June 15, 2011. The objective of GASB 64 is to provide clarification of whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. Utilities adopted GASB 64 effective January 1, 2012. There was no impact to the financial statements as a result of this implementation.

GASB Statement No. 63 *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* ("GASB 63") was issued in June 2011 effective for periods beginning after December 15, 2011. GASB 63 provides guidance on reporting deferred inflows and outflows of resources. The statement standardizes the presentation of deferred inflows and outflows of resources and their effect on government's net position. Utilities adopted GASB 63 effective January 1, 2012. Other than change in presentation, there was no impact to the financial statements as a result of this implementation.

#### ***GASB Pronouncement Implementations in the Future***

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions* ("GASB 68"), was issued in June 2012 effective for fiscal years beginning after June 15, 2014. The objective of GASB 68 is to amend the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of GASB Statement No. 50, *Pension Disclosures*, as they relate to governmental employers that account for pensions that are provided through trusts, or equivalent arrangements. Employers are required to report the difference between the actuarial total pension liability and the pension plan's fiduciary net position as the net pension liability on the Statements of Net Position. Previously, a liability was recognized only to the extent that contributions made to the plan were exceeded by the actuarially calculated annual required contributions. Utilities is currently assessing the adoption of GASB 68 and the impact it will have on its financial statements.

The GASB has also approved GASB Statement No. 66, *Technical Corrections - 2012 an amendment of GASB Statements No. 10 and No. 62*; Statement No. 67, *Financial Reporting for Pension Plans - an amendment of GASB Statement No. 25*; Statement No. 69, *Government Combinations and Disposals of Government Operations*; and Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantee Transactions*. Utilities does not anticipate the adoption of these standards will significantly impact the financial statements.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### ***USE OF ESTIMATES***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

#### ***FINANCIAL STATEMENT PRESENTATION***

Comparative total data for the prior year has been presented in the accompanying financial statements in order to provide an understanding of changes in the reporting entity's financial position and operations. Certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year's presentation.

#### ***DEPOSITS AND INVESTMENTS***

For purposes of the Statements of Cash Flows, cash and cash equivalents have original maturities of three months or less from the date of acquisition. Investment of funds is restricted by state statute.

Investments are limited to:

- Securities issued by, fully guaranteed by or for which the full credit of the United States Treasury is pledged for payment and which matures within five years of settlement
- Securities issued by, fully guaranteed by or for which the full credit of the following pledged for payment: the Federal Farm Credit Bank, the Federal Land Bank, a Federal Home Loan Bank, the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, the Export-Import Bank, the Tennessee Valley Authority, the World Bank or other comparable federal government sponsored agencies and that matures within five years of settlement
- Securities that are a general obligation of any U.S. state, the District of Columbia or any territorial possession of the U.S. and that are rated in one of its two highest rating categories by two or more nationally recognized organizations that regularly rate such obligations
- Securities that are a revenue obligation of any U.S. state, the District of Columbia, or any territorial possession of the U.S. and that are rated in its highest rating category by two or more nationally recognized organizations that regularly rate such obligations and that mature within three years of settlement
- Securities of the investing public entity
- Any interest in any local government investment pool, subject to various conditions
- Repurchase agreements, subject to various conditions
- Reverse repurchase agreements, subject to various conditions
- Securities lending agreement, subject to various conditions
- Any money market fund that is registered as an investment company under the federal Investment Company Act of 1940, subject to various conditions
- Any guaranteed investment contract that, at the time the contract or agreement is entered into, is rated in one of the two highest rating categories by two or more nationally recognized rating agencies that regularly issue such ratings
- Any corporate or bank security that is denominated in U.S. dollars, that matures within three years of settlement, that at the time of purchase carries at least two credit ratings from any of the nationally recognized statistical ratings organizations, with minimum rating requirements and other various conditions

Utilities has adopted an investment policy. That policy follows the state statute for allowable investments. Investments are stated at fair value, that is the amount at which an investment could be exchanged in a

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

current transaction between willing parties. Fair values are based on quoted market prices. No investments are reported at amortized cost. Adjustments necessary to record investments at fair value are recorded in the financial statements as increases or decreases in investment income. Market values may have changed significantly after year end.

#### ***RECEIVABLES AND PAYABLES***

Accounts receivable as of December 31, 2013 and 2012, include unbilled customers' accounts of \$40,850,212 and \$48,153,897, respectively. Accounts receivable has been reduced by an allowance for uncollectible accounts of \$2,924,846 and \$2,263,195 as of December 31, 2013 and 2012, respectively.

Outstanding balances between Utilities and the City are reported as "Due to or Due from other City funds."

Accounts payable are obligations to pay for goods or services purchased from suppliers in accordance with general course of business. Accounts payables are classified as current liabilities if payment is due within the next 12 months.

#### ***INVENTORIES AND PREPAID EXPENSES***

Inventories are valued at average cost. The cost of inventories are recorded as expenditures when consumed rather than when purchased. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses in the financial statements.

#### ***RESTRICTED ASSETS***

Debt proceeds available for the acquisition, construction, or improvement of capital assets that are unspent at year end are classified as restricted noncurrent assets.

Utilities' Bond Ordinances require individual reserve funds by bond issue, but allow Utilities to use surety bonds in lieu of cash bond reserve funds. The Bond Ordinances require that monies be restricted in separate accounts for the retirement of principal and payment of interest.

Under terms of International Swaps and Derivatives Association ("ISDA"), agreements covering interest rate and energy hedge positions held between Utilities and various counterparties, secured parties, are entitled to hold posted collateral directly or through a custodian. The value or amount of collateral posted is subject to thresholds and counterparty credit ratings established in the ISDA. Cash collateral held directly by Utilities is classified as a restricted noncurrent asset. The corresponding liability is classified as noncurrent on the Statements of Net Position.

#### ***CAPITAL ASSETS***

The costs of additions and replacements of assets identified as units of property or intangible assets that exceed \$5,000 and have an estimated useful life greater than one year are capitalized pursuant to Utilities' Capital Policy. Maintenance and replacement of minor items of property are charged to operating expense. When depreciable plant is retired, retirements are recorded against accumulated depreciation and the retired portion of depreciable plant is removed from plant in service. The net difference plus costs of removal and less salvage value, if any, are recorded to Nonoperating Revenues (Expenses) on the Statements of Revenues, Expenses and Changes in Net Position.

Utility plant is stated at the cost of construction, including expenditures for contracted services, direct labor and materials, indirect charges for engineering, labor burden, supervision, general and administrative expense and capitalized interest. Capitalized interest is applied to projects that require 30

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

days or more to complete. The 2013 and 2012 capitalized interest rate of 4.13% and 4.27%, respectively, are comprised of an interest rate on borrowed funds component and is applied to all major capital projects. Southern Delivery System (“SDS”) interest is directly capitalized to the project.

Utilities computes depreciation and amortization on plant in service on a straight-line, service-life basis. Depreciation is calculated using the following estimated service lives for major asset classifications:

	<u>Years</u>
Electric boiler plant/station equipment	25
Electric underground conduit	28.5
Gas mains and services	80
Water source of supply	100
Water treatment plant	25
Water transmission and distribution mains	50
Sewer mains and laterals	100
Wastewater preliminary treatment facility	45
General structures and improvements	57

#### **LEASES**

Utilities had no capital leases in 2013 and 2012.

#### **OTHER ASSETS**

Other assets are comprised primarily of a noncurrent asset acquisition adjustment that is being amortized over a 30 year period; equivalent to the remaining useful life of a natural gas fired combined cycle electric generation asset acquired in 2010.

In addition, SDS mitigation, engineering and design expenditures specific to monetary mitigation that do not meet Utilities’ capitalization requirements are recognized as a regulatory asset in other assets and are being amortized over a 10 year period. Utilities debt issuance costs are also included as a regulatory asset in the other assets balance. These are costs incurred to issue new or refunding debt, and include closing, legal and other costs required to issue debt. Debt issuance costs are amortized over the life of the bonds using the straight-line method and the expense is reported as other expense on the Statements of Revenues, Expenses and Changes in Net Position.

Utilities entered into a prepaid solar power purchase agreement in order to provide renewable solar photovoltaic electric energy service to the United States Air Force Academy. The prepaid amount is reported in other assets, reduced over time through actual usage.

#### **DERIVATIVE INSTRUMENTS**

Utilities utilizes financial derivatives to manage exposure to fluctuating natural gas prices and interest rates. All financial derivatives are stated at fair value as of December 31, 2013 and 2012, based on quoted market prices, current market conditions or other estimates obtained from third party broker dealers or valuation services.

#### **DEFERRED CASH FLOW HEDGES - UNREALIZED GAIN / LOSS ON DERIVATIVES**

Derivative instruments deemed effective by applying methods of evaluating effectiveness pursuant to GASB Statement No.53, *Accounting and Financial Reporting for Derivative Instruments* (“GASB 53”), are



## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

recognized as cash flow hedges. Changes in the fair value of cash flow hedge derivative instruments are reported as either a deferred cash flow hedge asset or liability on the Statements of Net Position.

#### ***CUSTOMER DEPOSITS***

Utilities accrues a liability for all amounts deposited by customers as security for the payment of bills.

#### ***COMPENSATED ABSENCES***

Utilities' employees earn vacation and sick leave in varying amounts. The amount of accumulated, unpaid vacation at year end is accrued and reported on the Statements of Net Position. Sick leave benefits which are anticipated to result in payments upon retirement are also accrued and reported on the Statements of Net Position.

#### ***CUSTOMER ADVANCES FOR CONSTRUCTION***

Utilities accrues a liability for advances by customers for construction which are to be refunded either wholly or in part.

#### ***LONG-TERM OBLIGATIONS***

Bond premiums and discounts are amortized over the life of the bond issues using the straight-line method which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount.

Additionally, any difference between the carrying amount of redeemed or defeased debt and its reacquisition price is deferred and amortized to interest expense using the straight-line method over the remaining life of the old debt or the life of the new debt, whichever is shorter.

#### ***MUNICIPAL SOLID WASTE LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS***

Utilities accrues a liability for its solid waste landfill closure and postclosure care costs. The liability is determined by multiplying the closure and postclosure care costs in current dollars by the percent capacity of the landfill used. Every five years, Utilities performs an independent assessment of post-closure landfill cost estimates and adjusts liabilities and expense recognition for any material differences. The last independent assessment was performed in 2012.

#### ***OTHER LIABILITIES***

Utilities recognizes future obligations associated with net insurance reserves, other post-employment benefits and unearned revenue.

#### ***NET POSITION***

***Net Investment in Capital Assets*** - This component of net position consists of capital assets net of accumulated depreciation and amortization and reduced by the outstanding balances of any bonds, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

***Restricted*** - This component of net position consists of constraints placed on net position use through external constraints imposed by creditors (such as through debt covenants), contributors, law, regulations of other governments, constraints imposed by law through constitutional provisions or enabling legislation.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

**Unrestricted** - This component of net position consists of amounts that do not meet the definition of “restricted” or “net investment in capital assets.” When an expense is incurred for purposes for which both restricted and unrestricted net position are available, it is Utilities’ policy to use a combination of restricted resources and unrestricted resources as they are needed.

#### **REVENUES AND EXPENSES**

Utilities distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering services in connection with Utilities’ principal ongoing operations. The principal operating revenues of Utilities are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses and depreciation and amortization on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Operating revenues are comprised of the following for year ended December 31:

	2013		2012	
	Amount	Percent	Amount	Percent
	(in thousands)			
Electric	\$ 416,442	49.6 %	\$ 416,231	47.8 %
Streetlight	4,250	0.5	3,921	0.5
Gas	207,773	24.8	207,096	23.7
Water	143,051	17.0	173,530	20.0
Wastewater	65,303	7.8	66,680	7.7
Products and services	2,188	0.3	2,196	0.3
Total	\$ 839,007	100.0 %	\$ 869,654	100.0 %
Less: Interdepartmental sales	(15,248)		(19,908)	
Total Operating Revenues	\$ 823,759		\$ 849,746	

Note: Immaterial differences may occur due to rounding.

#### **CAPITAL CONTRIBUTIONS**

Cash and capital assets are contributed to Utilities from customers, the City or external parties. The value of capital contributed to Utilities is reported as revenue on the Statements of Revenues, Expenses and Changes in Net Position.

#### **NOTE 3 - DEPOSITS AND INVESTMENTS**

The Federal Deposit Insurance Corporation standard insurance amount is \$250,000 per depositor, per insured bank, for each account ownership category (Tax ID). Coverage includes checking and savings accounts (interest bearing and noninterest bearing).

#### **DEPOSITS**

The Colorado Public Deposit Protection Act requires that financial institutions pledge a single institution pool of collateral against all the uninsured public deposits it holds and the market value of the securities in the pool is required to be in excess of 102% of the financial institution’s total uninsured public deposits.

As of December 31, 2013, the carrying amount of Utilities’ cash deposits was \$315,312,350. Petty cash was \$8,000 and the bank balance was \$341,153,785. A portion of the bank balance in the amount of

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

\$252,033 was covered by federal depository insurance and \$340,901,752 was collateralized as required by Colorado Statutes.

As of December 31, 2012, the carrying amount of Utilities' cash deposits was \$345,737,572. Petty cash was \$9,200 and the bank balance was \$358,170,561. A portion of the bank balance in the amount of \$36,188,551 was covered by federal depository insurance and \$321,982,010 was collateralized as required by Colorado Statutes.

#### **INVESTMENTS**

Utilities' investment policy is dictated by the Bond Ordinances for individual issues. These Bond Ordinances require Utilities to establish and maintain certain restricted investment funds, including unrestricted funds and reserve funds. Utilities is authorized to invest in any securities or other instruments permitted as investments of money of Utilities under the laws of the State. Utilities' investments are subject to interest rate, credit, concentration of credit and custodial credit risk as described below.

**Interest Rate Risk** - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. As a means of limiting its exposure to fair value losses arising from rising interest rates, Utilities' practice generally limits investments of its unrestricted funds to maturities of two years or less.

Utilities' investment balances as of December 31:

	2013		2012	
	Fair Value	Weighted Average Maturity in Years	Fair Value	Weighted Average Maturity in Years
	(in thousands)			
U.S. Treasury Notes	\$ 34,943	1.75	\$ 19,024	1.14
U.S. Government Agency Securities	79,837	1.47	47,154	2.03
Repurchase Agreements	10,313	0.00	16,614	0.00
Local Government Investment Pools	-	0.00	90	0.00
Total Investments	125,093		82,882	
Portfolio Weighted Average Maturity		1.43		1.42
Reconciliation to Total Cash and Investments				
Add:				
Cash on Hand and in Banks	308,719		294,946	
Cash with Fiscal Agent	6,601		50,801	
Total Cash and Investments	\$ 440,413		\$ 428,629	

Note: Immaterial differences may occur due to rounding.

**Credit Risk** - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. Pursuant to Utilities' Financial Risk Management Policy, all counterparties in swap or other financial products agreements with Utilities must have a long-term credit rating of "A-" issued by at least one major credit rating agency at the time of execution of such swap or financial products agreement, though there is no requirement that such a rating be maintained throughout the life of the financial products agreement. In the alternative, a counterparty must provide a guarantee, swap surety or other form of credit enhancement such that its enhanced creditworthiness is "A-" at the time of execution of

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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such swap or financial products agreement. The Financial Risk Management Policy also contains provisions which limit counterparty exposure.

As of December 31, 2013 and 2012, Utilities invested \$0 and \$89,846, respectively, in the Colorado Surplus Asset Fund Trust (“CSAFE”), an investment vehicle established for local government entities in Colorado pursuant to Part 7 of Article 75 of Title 24 of the Colorado Revised Statutes. The funds in CSAFE were expended in January 2013 and the investment account was closed as of January 31, 2013.

As of December 31, 2013 and 2012, Utilities invested \$10,313,490 and \$16,614,709, respectively, in repurchase agreements. Underlying investments related to the repurchase agreements were in U.S. Agency securities and other Government Sponsored Enterprises which carry an implied “AAA” credit rating.

Utilities’ investment ratings at December 31:

Investment Type	Moody's		S&P		Fitch	
	2013	2012	2013	2012	2013	2012
U.S. Government Treasury Securities	Aaa	Aaa	AA+	AA+	AAA	AAA
U.S. Government Agency Securities	Aaa	Aaa	AA+	AA+	AAA	AAA
Local Government Investment Pools	Not Rated	Not Rated	AAAm	AAAm	Not Rated	Not Rated
Repurchase Agreements	Not Rated	Not Rated	Not Rated	Not Rated	Not Rated	Not Rated

**Concentration of Credit Risk** - Concentration of credit risk is the risk of loss attributed to the magnitude of a government’s investment in a single issuer. Utilities, as an enterprise of a municipal government, places no limit on the amount that may be invested in a single issuer.

As of December 31, 2013, Utilities was invested in the following: \$27,140,190 in Federal National Mortgage Association securities, representing 21.7% of Utilities’ total investments; \$20,639,906 in Federal Home Loan Bank securities, representing 16.5% of Utilities’ total investments; \$28,053,208 in Federal Home Loan Mortgage Corporation securities, representing 22.4% of Utilities’ total investments; \$34,942,889 in U.S Treasury Notes, representing 27.9% of Utilities’ total investments; \$4,003,264 in Federal Farm Credit Banks, representing 3.2% of Utilities’ total investments; and \$10,313,490 of bond proceeds in a repurchase agreement with Bayerische Landesbank representing 8.3% of Utilities’ total investments.

As of December 31, 2012, Utilities was invested in the following: \$17,050,014 in Federal National Mortgage Association securities, representing 20.6% of Utilities’ total investments; \$6,020,986 in Federal Home Loan Bank securities, representing 7.3% of Utilities’ total investments; \$20,080,188 in Federal Home Loan Mortgage Corporation securities, representing 24.2% of Utilities’ total investments; \$19,024,146 in U.S Treasury Notes, representing 23.0% of Utilities’ total investments; \$4,002,808 in Federal Farm Credit Banks, representing 4.8% of Utilities’ total investments; and \$16,614,709 of bond proceeds in a repurchase agreement with Bayerische Landesbank, representing 20.1% of Utilities’ total investments.

**Custodial Credit Risk** - Utilities does not have any investments that are exposed to custodial credit risk.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

The deposits and investments reconcile to cash and cash equivalents and investments reported on the Statements of Net Position as of December 31, 2013:

	Cash and Cash Equivalents		Investments	
	Unrestricted	Restricted	Unrestricted	Restricted
	(in thousands)			
Deposits	\$ 111,031	\$ 202,851	\$ -	\$ 1,431
Petty Cash	8	-	-	-
Investments				
Repurchase Agreements	-	10,313	-	-
U.S. Treasury Notes	-	-	34,943	-
U.S. Government Agency Securities	-	-	79,836	-
<b>Total</b>	<b>\$ 111,039</b>	<b>\$ 213,164</b>	<b>\$ 114,779</b>	<b>\$ 1,431</b>

Note: Immaterial differences may occur due to rounding.

The deposits and investments reconcile to cash and cash equivalents and investments reported on the Statements of Net Position as of December 31, 2012:

	Cash and Cash Equivalents		Investments	
	Unrestricted	Restricted	Unrestricted	Restricted
	(in thousands)			
Deposits	\$ 111,670	\$ 232,585	\$ -	\$ 1,483
Petty Cash	9	-	-	-
Investments				
Repurchase Agreements	-	16,614	-	-
U.S. Treasury Notes	-	-	19,024	-
U.S. Government Agency Securities	-	-	47,154	-
CSAFE	-	90	-	-
<b>Total</b>	<b>\$ 111,679</b>	<b>\$ 249,289</b>	<b>\$ 66,178</b>	<b>\$ 1,483</b>

Note: Immaterial differences may occur due to rounding.

The amount of unrealized loss on investments included in investment income on the Statements of Revenue, Expenses and Changes in Net Position for the year ended December 31, 2013 and 2012 were \$33,093 and \$1,264, respectively.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### NOTE 4 - CAPITAL ASSETS

##### **SUMMARY OF CAPITAL ASSETS NET OF ACCUMULATED DEPRECIATION AND AMORTIZATION**

In September 2013, significant rainfall and flooding occurred in Utilities' service and surrounding areas. These events caused significant damage to some of the Utilities' infrastructure and assets, including some which were permanently impaired. Additional information is included in Note 19.

Summary for the year ended December 31, 2013:

	Beginning Balance	Additions	Deletions	Ending Balance
	(in thousands)			
Plant in Service				
Non-Depreciable Capital Assets				
Land	\$ 150,490	\$ -	\$ (217)	\$ 150,273
Intangible assets				
Land rights	13,321	1,599	-	14,920
Total Non-Depreciable Capital Assets	<u>163,811</u>	<u>1,599</u>	<u>(217)</u>	<u>165,193</u>
Depreciable Capital Assets				
Electric	1,761,946	63,854	(8,849)	1,816,951
Streetlight	41,263	1,525	-	42,788
Gas	293,851	10,212	(277)	303,786
Water and Wastewater	1,931,787	30,240	(1,288)	1,960,739
Common	285,917	5,264	(794)	290,387
Intangible assets				
Software	36,116	5,452	-	41,568
Land rights	44	-	-	44
Total Depreciable Capital Assets	<u>4,350,924</u>	<u>116,547</u>	<u>(11,208)</u>	<u>4,456,263</u>
Total Plant in Service	<u>4,514,735</u>	<u>118,146</u>	<u>(11,425)</u>	<u>4,621,456</u>
Accumulated Depreciation and Amortization				
Electric	(905,333)	(55,969)	3,863	(957,439)
Streetlight	(23,862)	(1,176)	-	(25,038)
Gas	(86,857)	(5,949)	268	(92,538)
Water and Wastewater	(579,475)	(37,873)	992	(616,356)
Common	(155,173)	(8,995)	779	(163,389)
Intangible assets				
Software	(20,107)	(6,562)	-	(26,669)
Land rights	(2)	(2)	-	(4)
Total Accumulated Depreciation and Amortization	<u>(1,770,809)</u>	<u>(116,526)</u>	<u>5,902</u>	<u>(1,881,433)</u>
Total Plant in Service (net of Accumulated Depreciation and Amortization)	<u>2,743,926</u>	<u>1,620</u>	<u>(5,523)</u>	<u>2,740,023</u>
Construction work in progress	<u>460,110</u>	<u>290,538</u>	<u>(102,470)</u>	<u>648,178</u>
Total Capital Assets (net of Accumulated Depreciation and Amortization)	<u>\$ 3,204,036</u>	<u>\$ 292,158</u>	<u>\$ (107,993)</u>	<u>\$ 3,388,201</u>

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

Summary for the year ended December 31, 2012:

	Beginning Balance	Additions	Deletions	Ending Balance
	(in thousands)			
Plant in Service				
Non-Depreciable Capital Assets				
Land	\$ 150,372	\$ 118	\$ -	\$ 150,490
Intangible assets				
Land rights	11,949	1,393	(21)	13,321
Total Non-Depreciable Capital Assets	<u>162,321</u>	<u>1,511</u>	<u>(21)</u>	<u>163,811</u>
Depreciable Capital Assets				
Electric	1,694,224	70,669	(2,947)	1,761,946
Streetlight	40,245	1,023	(5)	41,263
Gas	282,567	12,265	(981)	293,851
Water and Wastewater	1,900,115	34,774	(3,102)	1,931,787
Common	281,092	6,460	(1,635)	285,917
Intangible assets				
Software	28,974	7,142	-	36,116
Land rights	44	-	-	44
Total Depreciable Capital Assets	<u>4,227,261</u>	<u>132,333</u>	<u>(8,670)</u>	<u>4,350,924</u>
Total Plant in Service	<u>4,389,582</u>	<u>133,844</u>	<u>(8,691)</u>	<u>4,514,735</u>
Accumulated Depreciation and Amortization				
Electric	(853,143)	(54,726)	2,536	(905,333)
Streetlight	(22,700)	(1,166)	4	(23,862)
Gas	(81,921)	(5,849)	913	(86,857)
Water and Wastewater	(543,770)	(37,639)	1,934	(579,475)
Common	(147,925)	(8,918)	1,670	(155,173)
Intangible assets				
Software	(14,160)	(5,958)	11	(20,107)
Land rights	(1)	(1)	-	(2)
Total Accumulated Depreciation and Amortization	<u>(1,663,620)</u>	<u>(114,257)</u>	<u>7,068</u>	<u>(1,770,809)</u>
Total Plant in Service (net of Accumulated Depreciation and Amortization)	<u>2,725,962</u>	<u>19,587</u>	<u>(1,623)</u>	<u>2,743,926</u>
Construction work in progress	<u>335,831</u>	<u>246,153</u>	<u>(121,874)</u>	<u>460,110</u>
Total Capital Assets (net of Accumulated Depreciation and Amortization)	<u>\$ 3,061,793</u>	<u>\$ 265,740</u>	<u>\$ (123,497)</u>	<u>\$ 3,204,036</u>

Note: Immaterial differences may occur due to rounding.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### **NOTE 5 - DERIVATIVE INSTRUMENTS**

Utilities' financial derivatives are acquired with the objective of effectively hedging expected cash flows. Interest rate and natural gas hedges that are deemed effective, by applying methods of evaluating effectiveness pursuant to GASB 53 are recognized as cash flow hedges. Some financial derivatives do not meet the criteria for effectiveness and therefore are classified as investment derivatives. Changes in the fair value of cash flow hedge derivative instruments are reported as either a deferred outflow or inflow of resources on the Statements of Net Position. Interest rate and natural gas hedges that are deemed ineffective are recognized as standalone investment derivatives. The change in the fair value of investment derivatives is recognized as nonoperating revenue or expense on the Statements of Revenues, Expenses and Changes in Net Position.

Utilities has interest rate hedges based on both the Securities Industry and Financial Markets Association ("SIFMA") index and the London Interbank Offered Rate ("LIBOR") index. Utilities' interest rate derivatives based on 68% of 1-month LIBOR were classified as cash flow hedges. As of December 31, 2013, these derivatives are no longer effective pursuant to GASB 53 hedge effectiveness standards and are considered investment derivatives.

Utilities also evaluates physical supply contracts for compliance with the Normal Purchase and Sales Exemption pursuant to GASB 53. Utilities had a large physical supply contract for coal in which both the terms of this contract and Utilities' action regarding delivery of this contract met the criteria of a Normal Purchase and Sales Exemption from the contract inception date through year end 2009. During 2010, a significant amount of contractual volumes were net settled with the supplier at Utilities' initiative to allow for more economic consumption of coal from alternative sources, thereby reducing delivery of the coal to designated generation facilities under this contract. As a result, the Normal Purchase and Sales Exemption was no longer applicable. As of December 31, 2010, this contract was evaluated as a derivative instrument and deemed ineffective due to the classification of the underlying physical notional volume and price as a financial derivative, precluding the ability to perform hedge effectiveness testing against another derivative. The contract terminated in December 2012.

Utilities values interest rate derivatives based on valuations provided by DerivActiv, L.L.C., an independent third party valuation service provider. Natural gas swap derivatives are valued using published pricing benchmarks obtained through independent sources or financial institutions dealing in these markets. Natural gas option derivatives are valued based on monthly quoted prices from approved counterparties. The fair values of the interest rate and natural gas derivatives are based on present value of their estimated future cash flows.

#### ***INTEREST RATE SWAP NOVATIONS***

In May 2012, Utilities replaced its swap counterparty on two bond issues totaling \$149.8 million. These swap novations resulted in \$39.3 million in collateral relief to Utilities, an increase in unrestricted cash balances, reduced counterparty exposure to European financial institutions and increased diversification of the swap portfolio.



## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### **SUMMARY OF DERIVATIVE INSTRUMENTS**

The fair values and notional amounts of derivative instruments outstanding at December 31, 2013, classified by type and changes in fair value of such derivative instruments for the year then ended:

	2013 Changes in Fair Value		Fair Value at December 31, 2013		Notional
	Classification	Amount	Classification	Amount	
			(in thousands)		
<u>Cash flow hedges</u>					
Interest Rate Swaps	Deferred outflows	\$ 153,637	Derivative instruments	\$ (47,042)	\$ 225,855
Commodity Derivatives:					
Swap contracts	Deferred outflows	11,866	Derivative instruments	(194)	116,000 MMBtu
Option Structures	Deferred outflows	235	Derivative instruments	-	
Total Cash Flow Hedges		<u>\$ 165,738</u>		<u>\$ (47,236)</u>	
<u>Investment derivative</u>					
Interest Rate Swaps	Derivative gain/(loss)	\$ (67,936)	Derivative instruments	\$ (90,443)	\$ 462,425
Total Investment Derivative		<u>\$ (67,936)</u>		<u>\$ (90,443)</u>	

Note: Immaterial differences may occur due to rounding.

The fair values and notional amounts of derivative instruments outstanding at December 31, 2012, classified by type and changes in fair value of such derivative instruments for the year then ended:

	2012 Changes in Fair Value		Fair Value at December 31, 2012		Notional
	Classification	Amount	Classification	Amount	
			(in thousands)		
<u>Cash flow hedges</u>					
Interest Rate Swaps	Deferred outflows	\$ 769	Derivative instruments	\$ (200,679)	\$ 591,906
Commodity Derivatives:					
Swap contracts	Deferred outflows	40,545	Derivative instruments	(12,060)	5,929 MMBtu
Option Structures	Deferred inflows	(142)	Derivative instruments	(235)	3,744 MMBtu
Total Cash Flow Hedges		<u>\$ 41,172</u>		<u>\$ (212,974)</u>	
<u>Investment derivative</u>					
Interest Rate Swaps	Derivative gain/(loss)	\$ (610)	Derivative instruments	\$ (22,507)	\$ 112,255
Commodity Derivatives:					
Swap contracts	Derivative gain/(loss)	(76)	Derivative instruments	-	
Coal contract	Derivative gain/(loss)	6,862	Derivative instruments	-	
Total Investment Derivative		<u>\$ 6,176</u>		<u>\$ (22,507)</u>	

Note: Immaterial differences may occur due to rounding.

The pay-fixed, receive variable interest rate swap is a type of derivative utilized by Utilities that is designed to synthetically fix the cash flows on the variable rate demand obligation bonds ("VRDO"). The variable rate received on the interest rate swaps is intended to offset the variable rate being paid on the obligations so that the fixed rate of the swap is essentially the effective rate incurred by Utilities.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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Two primary types of commodity derivative instruments are utilized in Utilities' natural gas hedging program: fixed price forward swaps and option structures. These derivative agreements are designed to stabilize cash flow due to market price fluctuations related to expected purchases of natural gas. Utilities entered into option structures to manage natural gas price exposure above or below a designated strike price. As of December 31, 2013, Utilities has no natural gas derivatives in place to hedge 2014 natural gas exposures. Natural gas hedging activities for 2014 and beyond have been suspended pending results of an ongoing program evaluation.

Summary of scheduled projected future cash flows for interest rate derivatives as of December 31, 2013:

<u>December 31,</u>	<u>Projected Future Cash Flows In/(Out) for Hedging Derivatives</u>
	<u>(in thousands)</u>
2014	\$ (25,383)
2015	(25,030)
2016	(24,624)
2017	(24,183)
2018	(23,710)
2019-2023	(110,216)
2024-2028	(69,039)
2029-2033	(29,912)
2034-2038	(10,067)
2039-2041	(866)
	<u>\$ (343,030)</u>

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

Summary of Utilities' pay-fixed interest rate swap agreements outstanding as of December 31, 2013:

	Notional Amount (in thousands)	Effective Date	Maturity Date	Terms	Counterparty
<u>Cash flow hedges</u>					
2005 SIFMA Swap	\$ 69,639	09/15/05	11/01/35	Pay 4.7099%; receive SIFMA index	Bank of America, N.A
2005 SIFMA Swap	23,356	09/15/05	11/01/35	Pay 4.7099%; receive SIFMA index	J. Aron & Co.
2007 Refunding SIFMA Swap (2012 Novation)	87,275	10/01/07	11/01/26	Pay 5.295%; receive SIFMA index	The Bank of New York Mellon
2008 SIFMA Swap	45,585	09/12/08	11/01/38	Pay 4.2686%; receive SIFMA index	Bank of America, N.A
<u>Investment derivative</u>					
2004 SIFMA Swap	103,725	08/18/04	11/01/23	Pay 4.1120%; receive SIFMA index	JP Morgan Chase Bank
2005 SIFMA Swap	430	09/15/05	11/01/35	Pay 4.7099%; receive SIFMA index	Bank of America, N.A
2006 Refunding LIBOR Swap	60,625	08/24/06	11/01/25	Pay 4.4810%; receive 68% of LIBOR	JP Morgan Chase Bank
2006 New Money LIBOR Swap	43,155	09/14/06	11/01/36	Pay 4.1185%; receive 68% of LIBOR	Morgan Stanley Capital Group Inc.
2006 New Money LIBOR Swap	28,770	09/14/06	11/01/36	Pay 4.1185%; receive 68% of LIBOR	JP Morgan Chase Bank
2007 New Money LIBOR Swap	41,280	09/13/07	11/01/37	Pay 3.198%; receive 68% of LIBOR	J. Aron & Co.
2007 New Money LIBOR Swap	27,520	09/13/07	11/01/37	Pay 3.198%; receive 68% of LIBOR	Morgan Stanley Capital Group Inc.
2009 LIBOR Swap (2012 Novation)	61,475	10/01/09	11/01/28	Pay 5.475%; receive 68% of LIBOR	Wells Fargo Bank, N.A.
2010 LIBOR Swap	47,240	10/26/10	11/01/40	Pay 3.8807%; receive 68% of LIBOR	Morgan Stanley Capital Group Inc.
2012 LIBOR Swap	48,205	03/15/12	11/01/41	Pay 4.0242%; receive 68% of LIBOR	Morgan Stanley Capital Group Inc.
Total Notional Amount for Interest Rate Swaps	<u>\$ 688,280</u>				

Note: Immaterial differences may occur due to rounding.

**2004 SIFMA Swap** - If SIFMA averages more than 7% for 180 consecutive calendar days during the term of the 2004 SIFMA Swap, the 2004 SIFMA Swap will terminate by its terms and no payments by either party will be due.

**2005 SIFMA Swap** - During fourth quarter 2012, it was discovered that in 2008 Utilities redeemed a portion of its 2005A variable rate bond series through the issuance of the 2008D Clean Renewable

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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Energy Bonds (CREBs). This transaction created an immaterial difference between the notional size of the bond issuance and the interest rate swap hedge. The overhedged portion of the swap has therefore been declared an investment derivative.

Summary of Utilities' fixed price natural gas swap agreements outstanding as of December 31, 2013:

	Notional Amount MMBtu	Effective Date	Maturity Date	Terms
<u>Cash flow hedges</u>				
J. Aron & Co.	78,000	Dec-13	Dec-13	Pay Average \$6.067/MMBtu; settlement based on Cheyenne Daily pricing point at expiration date.
BP Energy Company	38,000	Dec-13	Dec-13	Pay Average \$6.465/MMBtu; settlement based on Cheyenne Daily pricing point at expiration date.
Total Notional Amount for Commodity Swaps	<u>116,000</u>			

Note: Immaterial differences may occur due to rounding.

Utilities' has no option structures outstanding as of December 31, 2013.

### **Risk**

Utilities routinely monitors and manages risks in the areas of Credit risk, Interest Rate risk and associated Basis risk, Natural Gas Price risk, Termination risk, Rollover risk, Market Access risk and Foreign Currency risk. These risks are discussed in detail below.

**Credit Risk** - Credit risk is the exposure resulting when the counterparty is unable or unwilling to fulfill its present and future financial obligations. Each of Utilities' interest rate or natural gas cash flow and investment derivative instruments are held with various counterparties of high credit quality. Utilities views counterparty credit risks that may arise through interest rate and natural gas derivative transactions as similar between cash flow hedges and investment derivatives.

Counterparty credit rating at December 31:

Counterparty	Credit Rating	
	2013	2012
BP Corporation North America Inc.	Baa1/A	Baa1/A
J. Aron & Co.	Baa1/A-	A3/A-
JP Morgan Chase Bank	Aa3/A+	Aa3/A+
Bank of America, N.A.	A2/A	A3/A
Morgan Stanley Capital Group Inc.	Baa2/A-	Baa1/A-
Wells Fargo Bank, N.A.	Aa3/AA-	Aa3/AA-
The Bank of New York Mellon	Aa2/AA-	Aa1/AA-

The Energy Risk Management Policy requires that Utilities' counterparties to commodity transactions be on an approved counterparty list. To be on this list, counterparties must have a minimum rating of "Baa2" issued by Moody's, a minimum rating of "BBB" issued by S&P, a minimum rating of "BBB" issued by Fitch,

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

or be specifically approved by Utilities' Risk Management Committee. The Energy Risk Management Policy limits the amount of counterparty credit exposure according to the counterparty's credit rating. To be on the interest rate counterparty transaction list, at the time of transaction execution, counterparties must have a minimum credit rating of "A-" category by at least one of the major credit rating agencies previously listed at the time of transaction or a counterparty shall provide a guarantee, swap surety, or other form of credit enhancement such that its creditworthiness is of an "A-" category equivalent. Each counterparty must also have a demonstrated record of successfully executing swap transactions and shall have a minimum capitalization of at least \$250.0 million.

It is Utilities' policy to require collateral posting provisions for all counterparties involved in its non-exchange-traded derivative instrument transactions. The collateral posted by counterparties is governed by ISDA agreements with collateral threshold limits as specified in each agreement. As the mark to market value of a fixed price financial derivative held by Utilities decreases relative to market, Utilities may be obligated to post collateral with the applicable counterparty. Conversely, as the mark to market value of a fixed price financial derivative agreement or call option increases, Utilities' counterparties may be required to post collateral.

At December 31, 2013, Utilities has posted approximately \$6.6 million in collateral with the various counterparties to the swap agreements. As of December 31, 2012, Utilities' collateral posting with all counterparties was \$50.8 million. Utilities' aggregate fair value of derivative instruments as of December 31, 2013, was approximately (\$137.7) million compared to (\$235.5) million at the end of 2012.

The combined fair value of all derivative instruments, net of collateral postings, as of December 31, 2013 and 2012 was approximately (\$131.1) million and (\$184.7) million, respectively.

Collateral postings represent the initial amount that Utilities would be required to pay in the event counterparties failed due to a credit default event. Collateral posted is presented as restricted cash and impacts Utilities' cash reserves and liquidity. In the event of a failure of all counterparties due to a credit default, Utilities anticipates the full value of the collateral posting would be liquidated on behalf of secured creditors, thereby reducing actual cash balances and liquidity by the value of the collateral posting. A credit default by all counterparties could lead to additional cash requirements called by secured creditors up to the net liability of the combined derivative positions.

The impact of a future credit default on Utilities is dependent on market conditions that exist at the time of the event. As a result, the impact on Utilities' cash and liquidity position could be negative or positive. In consideration of this uncertainty and to minimize the impact of such an event on liquidity, as of December 31, 2013, Utilities has total lines of credit available in the amount of \$75.0 million. Utilities also closely monitors the creditworthiness of all existing counterparties and awards future business based on creditworthiness and collateral positions existing at the time of the transaction.

**Interest Rate Risk** - Interest rate risk is the risk that changes in market interest rates will adversely affect Utilities' anticipated cash flows. Utilities is exposed to interest rate risk on its variable rate debt. Utilities utilizes fixed price swaps to offset cash flow exposures to variable rate debt. Utilities receives fixed rate swap payments against VRDOs based on SIFMA and LIBOR swap indices.

**Basis Risk** - Basis risk is the risk that arises when variable rates or prices of a derivative instrument and a hedged item are based on different reference rates. Utilities is exposed to basis risk on its pay-fixed interest rate swap hedging derivative instruments because the variable rate payments received by Utilities on these hedging derivative instruments are based on a rate or index other than interest rates. Utilities pays on its hedged variable rate debt, which is generally remarketed every 7 days. As of December 31, 2013, the weighted average interest rate on Utilities' variable rate debt was 0.077%, the SIFMA swap

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

index rate was 0.06%, while 68% of the LIBOR was 0.114%. As of December 31, 2012, the weighted average interest rate on Utilities' variable rate debt was 0.167%, the SIFMA swap index rate was 0.13%, while 68.0% of LIBOR was 0.143%.

**Natural Gas Price Risk** - Natural gas price risk is the risk that changes in natural gas market prices for physical delivery will adversely impact Utilities' anticipated cash flows. Utilities enters into fixed price swaps and options to offset anticipated natural gas price risks. The financial derivatives are priced identically to the underlying physical natural gas contracts, so that no basis risk exists.

**Termination Risk** - Termination risk is the risk that a derivative instrument's unscheduled end will affect Utilities' asset and liability strategy or will present Utilities with potentially unscheduled termination payments to the counterparty. Utilities or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract or if both parties agree to exercise a termination option. If at the time of termination, a hedging derivative instrument is in a liability position, Utilities would be liable to the counterparty for a payment equal to the liability, subject to netting arrangements.

**Rollover Risk** - Rollover risk is the risk that a derivative instrument associated with a hedged item does not extend to the maturity of that hedged item. Utilities is exposed to rollover risk on hedging instruments that are hedges of debt that mature or may be terminated prior to the maturity of the hedged debt. When these hedging derivative instruments terminate, or in case of a termination option, if a counterparty exercises its option, Utilities will be re-exposed to the risks being hedged by the hedging derivative instrument. Utilities has no exposure to rollover risk with current interest rate derivative instruments.

**Market Access Risk** - Market access risk is the risk that Utilities will not be able to enter credit markets or that credit will become more costly. A strong credit rating tends to broaden an entity's credit market access and bondholder base while achieving lower cost funding. As of December 2013 and 2012 Utilities' long-term credit rating is "Aa2/AA/AA" by Moody's, S&P and Fitch, respectively.

**Foreign Currency Risk** - Foreign currency risk is the risk that changes in exchange rates will adversely affect the cash flows of a transaction. Utilities has no exposure to foreign currency risk.

## COLORADO SPRINGS UTILITIES

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2013 and 2012

### NOTE 6 - TOTAL LONG-TERM DEBT

#### **SUMMARY OF SCHEDULED MATURITIES OF TOTAL LONG-TERM DEBT**

**Revenue Bonds** - scheduled maturities as of December 31, 2013:

<u>December 31,</u>	<u>Principal</u>	<u>Interest</u>
	(in thousands)	
2014	\$ 55,764	\$ 105,372
2015	59,954	102,850
2016	66,234	101,574
2017	69,590	100,163
2018	73,410	98,999
2019 - 2023	442,338	440,454
2024 - 2028	534,135	325,933
2029 - 2033	471,135	198,100
2034 - 2038	280,665	112,403
2039 - 2043	170,185	48,260
2044 - 2048	67,970	17,462
2049 - 2050	20,260	1,685
Total	<u>\$ 2,311,640</u>	<u>\$ 1,653,255</u>

Note: Immaterial differences may occur due to rounding.

**Notes and Loans Payable** - scheduled maturities as of December 31, 2013:

<u>December 31,</u>	<u>Principal</u>	<u>Interest</u>
	(in thousands)	
2014	\$ 1,531	\$ 582
2015	1,502	535
2016	2,402	476
2017	2,391	405
2018	2,465	301
2019 - 2023	4,370	634
2024 - 2028	2,441	304
2029 - 2030	1,065	33
Total	<u>\$ 18,167</u>	<u>\$ 3,270</u>

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### ***SUMMARY OF TOTAL LONG-TERM DEBT***

The following is a summary of the total long-term debt as of December 31, 2013:

	<u>Original Amount</u>	<u>Interest Rate Ranges/ Maturity Dates</u>	<u>Outstanding Principal at December 31, 2013</u>	<u>Future Aggregate Interest Requirements at December 31, 2013</u>
	(in thousands)			
<u>Revenue bonds</u>				
Utilities System Improvement Revenue Bonds, Series 2013B-2	\$ 68,645	2.000%-5.000% 2014-2043	\$ 68,645	\$ 65,556
Utilities System Improvement Revenue Bonds, Series 2013B-1	58,915	1.500%-5.000% 2014-2043	58,915	55,272
Utilities System Refunding Revenue Bonds, Series 2013A	97,580	1.500%-5.000% 2013-2045	97,580	73,566
Utilities System Refunding Revenue Bonds, Series 2012C	157,670	3.000%-5.000% 2013-2042	155,460	81,670
Utilities System Refunding Revenue Bonds, Series 2012B	108,015	3.000%-5.000% 2013-2043	107,830	64,187
Variable Rate Demand Utilities System Improvement Revenue Bonds, Series 2012A	50,000	4.024% 2012-2033	48,205	32,932
Utilities System Refunding Revenue Bonds, Series 2011A	167,490	2.000%-5.000% 2012-2033	143,955	59,544
Utilities System Revenue Bonds, Series 2010D	273,855	1.324%-6.615% 2011-2040	258,165	258,938
Variable Rate Demand Utilities System Improvement Revenue Bonds, Series 2010C	50,000	3.881% 2011-2040	47,240	29,854



## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

	<u>Original Amount</u>	<u>Interest Rate Ranges/ Maturity Dates</u>	<u>Outstanding Principal at December 31, 2013</u>	<u>Future Aggregate Interest Requirements at December 31, 2013</u>
	(in thousands)			
<u>Revenue bonds - continued</u>				
Utilities System Improvement and Taxable Utilities System Revenue Bonds, Series 2010B	\$ 180,000	3.397%-5.738% 2016-2050	\$ 180,000	\$ 234,276
Utilities System Revenue and Taxable Utilities System Improvement Revenue Bonds, Series 2010A	139,835	0.600%-5.467% 2011-2040	129,045	62,525
Taxable Utilities System Improvement Revenue Bonds, Series 2009D	56,750	4.164%-6.313% 2016-2049	56,750	80,425
Variable Rate Demand Utilities System Refunding Revenue Bonds, Series 2009C	66,455	5.475% 2010-2028	64,205	47,001
Utilities System Revenue and Taxable Utilities System Improvement Revenue Bonds, Series 2009B	82,000	4.000%-5.545% 2010-2039	76,210	64,193
Utilities System Refunding Revenue Bonds, Series 2009A	60,750	2.250%-5.000% 2010-2033	54,735	28,218
Utilities System Improvement and Refunding Clean Renewable Energy Bonds, Series 2008D	3,631	1.350% 2008-2021	2,075	126
Utilities System Improvement Revenue Bonds, Series 2008C	41,975	4.500%-5.500% 2013-2048	41,535	50,435
Utilities System Refunding Revenue Bonds, Series 2008B	27,935	3.000%-5.400% 2009-2033	24,065	14,122

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

	<u>Original Amount</u>	<u>Interest Rate Ranges/ Maturity Dates</u>	<u>Outstanding Principal at December 31, 2013</u>	<u>Future Aggregate Interest Requirements at December 31, 2013</u>
	(in thousands)			
<u>Revenue bonds - continued</u>				
Variable Rate Demand Utilities				
System Improvement				
Revenue Bonds,				
Series 2008A	\$ 50,000	4.269% 2009-2038	\$ 45,585	\$ 29,596
Utilities System Refunding				
Revenue Bonds,				
Series 2007C	24,415	4.000%-5.000% 2008-2022	16,285	3,507
Variable Rate Demand Utilities				
System Improvement and				
Refunding Revenue Bonds,				
Series 2007B	87,275	5.295% 2023-2026	87,275	52,346
Variable Rate Demand Utilities				
System Improvement				
Revenue Bonds,				
Series 2007A	75,000	3.198% 2008-2037	68,800	31,523
Variable Rate Demand Utilities				
System Subordinate Lien				
Improvement Revenue Bonds,				
Series 2006B	75,000	4.119% 2011-2036	71,925	42,398
Variable Rate Demand Utilities				
System Subordinate Lien				
Improvement and Refunding				
Revenue Bonds,				
Series 2006A	60,625	4.481% 2015-2025	60,625	29,079
Utilities System Subordinate				
Lien Improvement				
Revenue Bonds,				
Series 2005C	16,050	3.750%-5.125% 2012-2045	490	30
Utilities System Subordinate				
Lien Improvement				
Revenue Bonds,				
Series 2005B	19,240	3.500%-5.000% 2009-2035	1,005	72

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

	<u>Original Amount</u>	<u>Interest Rate Ranges/ Maturity Dates</u>	<u>Outstanding Principal at December 31, 2013</u>	<u>Future Aggregate Interest Requirements at December 31, 2013</u>
	(in thousands)			
<u>Revenue bonds - continued</u>				
Variable Rate Demand Utilities				
System Subordinate Lien				
Improvement Revenue Bonds,				
Series 2005A	\$ 100,000	4.710% 2010-2035	\$ 92,995	\$ 58,851
Utilities System Subordinate				
Lien Improvement				
Revenue Bonds,				
Series 2004C	15,695	4.000%-5.000% 2008-2044	230	9
Utilities System Subordinate				
Lien Improvement				
Revenue Bonds,				
Series 2004B	107,115	4.500%-5.500% 2008-2034	2,665	147
Variable Rate Demand Utilities				
Subordinate Lien Refunding				
Revenue Bonds,				
Series 2004A	117,450	4.112% 2010-2023	103,725	26,959
Utilities System Subordinate				
Lien Improvement				
Revenue Bonds,				
Series 2003B	45,000	3.000%-5.000% 2009-2043	675	26
Taxable Variable Rate Demand				
Utilities System Subordinate				
Lien Revenue Bonds,				
Series 2002C	27,055	0.170% 2027	27,055	14,824
Taxable Utilities System				
Subordinate Lien				
Revenue Bonds,				
Series 2000B	15,000	7.500% 2001-2020	7,690	2,473
Variable Rate Demand				
Utilities System Subordinate				
Lien Revenue Bonds,				
Series 2000A	110,000	0.150% 2029	110,000	58,575

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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	Original Amount	Interest Rate Ranges/ Maturity Dates	Outstanding Principal at December 31, 2013	Future Aggregate Interest Requirements at December 31, 2013
	(in thousands)			
<u>Notes and loans payable</u>				
2009 Drinking Water Revolving Fund				
Loan, Water Resources & Power				
Authority Improvement Bonds,				
Series 2009E	\$ 8,600	2.500%	\$ 7,566	\$ 1,768
		2011-2030		
Colorado Water Resources &				
Power Development Authority				
Clean Water Revenue Bonds,				
Series 1998B	22,204	3.700%-5.500%	10,601	1,502
		1999-2019		
Total Long-Term Debt			\$ 2,329,807	\$ 1,656,525

Note: Immaterial differences may occur due to rounding.

#### NOTE 7 - REVENUE BONDS

During 2013, Utilities issued \$97,580,000 Utilities System Refunding Revenue Bonds, Series 2013A, \$58,915,000 Utilities System Improvement Revenue Bonds, Series 2013B-1 and \$68,645,000 Utilities System Improvement Revenue Bonds, Series 2013B-2. These series and any subsequently issued and outstanding revenue bonds are equitably and ratably secured by a lien on net pledged revenues.

During 2012, Utilities issued \$50,000,000 Variable Rate Utilities System Improvement Revenue Bonds, Series 2012A, \$108,015,000 Utilities System Refunding Revenue Bonds, Series 2012B, \$113,565,000 Utilities System Revenue Bonds, Series 2012C-1 and \$44,105,000 Utilities System Revenue Bonds, Series 2012C-2. These series and any subsequently issued and outstanding revenue bonds are equitably and ratably secured by a lien on net pledged revenues.

The individual remarketing agents for the 2000A, 2002C, 2004A, 2005A, 2006A, 2006B, 2007A, 2007B, 2008A, 2009C, 2010C and 2012A VRDOs calculate weekly the interest rate to be paid to bondholders by determining the interest rate that would enable the bonds to be remarketed at par, plus accrued interest, if any.

Utilities has approximately 6.0% of total outstanding debt in VRDOs that are not hedged. This percentage does not include the following series of Utilities' outstanding bonds because each are part of a variable to fixed interest rate swap transaction, with the exception of the Series 2009C, as indicated below:

- Refunding Revenue Bonds, Series 2004A,
- Improvement Revenue Bonds, Series 2005A,
- Improvement and Refunding Revenue Bonds, Series 2006A,
- Improvement Revenue Bonds, Series 2006B,
- Improvement Revenue Bonds, Series 2007A,
- Improvement and Refunding Revenue Bonds, Series 2007B,
- Improvement Revenue Bonds, Series 2008A,

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

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- Refunding Revenue Bonds, Series 2009C (with the exception of \$2,730,000 in unhedged principal),
- Improvement Revenue Bonds, Series 2010C, or
- Improvement Revenue Bonds, Series 2012A

Pursuant to its Financial Risk Management Policy, Utilities is allowed to have outstanding up to 30.0% of its total outstanding debt in unhedged variable rate debt.

Revenue bonds constitute an irrevocable lien, but not necessarily an exclusive lien, upon net pledged revenues pursuant to the Bond Ordinances. All Utilities' revenues net of specified operating expenses are pledged as security for all revenue bonds and loans payable until they are defeased. None of the covenants, agreements, representations and warranties contained in the Ordinance or in the Bonds, nor the breach thereof, shall ever impose or shall be construed as imposing any liability, obligation or charge against the City (except the special funds pledged therefor), or against its general credit, or as payable out of its general fund or out of any funds derived from taxation or out of any other revenue source (other than those pledged therefor). The full faith and credit of the City is not pledged for the payment of the amounts due on the Bonds or under the Ordinance. Principal and interest paid for 2013 and 2012 was \$154,192,910 and \$151,142,496, respectively. Total net pledged revenues as defined for the same periods were \$319,515,816 in 2013 and \$337,801,583 in 2012. Annual principal and interest payments required 48.3% and 44.7% of net pledged revenues, respectively.

#### ***ARBITRAGE REBATE PAYABLE***

Section 148 of the Internal Revenue Code requires issuers of most types of tax-exempt bonds to rebate investment earnings in excess of bond yield to the United States Internal Revenue Service in installment payments made at least once every five years, with the final installment made when the last bond in the issue is redeemed.

The most recent arbitrage rebate analysis was completed as of December 31, 2013, by a consulting firm. Future computations of the rebate requirement on outstanding bond issues will be calculated annually, with an arbitrage rebate liability recorded for any issues that have a material amount due at the time of calculation.

Utilities bond issues do not carry any liability. The 2008A, 2008B, 2008C, 2009A, 2009B, 2009C, 2009D, 2010A, 2010B, 2010C, 2010D, 2011A, 2012A, 2012B and 2012C bond issues will continue to have annual calculations completed until no longer required. The 2000A, 2003B, 2004A, 2004B, 2004C, 2005A, 2005B, 2005C, 2006A, 2006B, 2007A, 2007B, 2007C and 2008D bond issues no longer require calculations.

#### ***CURRENT AND ADVANCE REFUNDING***

On April 15, 2013, the 2013A bonds were issued. The proceeds were used to refund portions of outstanding series 2004B, 2004C, 2005B and 2005C parity revenue bonds and funded the debt service reserve fund:

- \$51,235,000 was issued with an average interest rate of 3.482% to advance refund \$51,590,000 of outstanding 2004B bonds with an average interest rate of 4.922%. The net proceeds of \$56,496,300 (after payment of \$514,059 in bond issuance costs and \$1,221,026 debt service reserve fund) plus an additional \$1,269,088 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from

## COLORADO SPRINGS UTILITIES

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the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$98,121,700 from 2013 to 2034. The cash flow requirement on the new bonds is \$90,307,821 from 2013 through 2045. The advance refunding resulted in an economic gain of \$5,885,303. At December 31, 2013, \$51,590,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2014.

- \$14,510,000 was issued with an average interest rate of 3.582% to advance refund \$14,265,000 of outstanding 2004C bonds with an average interest rate of 4.782%. The net proceeds of \$15,547,420 (after payment of \$149,640 in bond issuance costs and \$393,432 debt service reserve fund) plus an additional \$332,334 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$28,425,506 from 2013 to 2044. The cash flow requirement on the new bonds is \$27,099,832 from 2013 through 2045. The advance refunding resulted in an economic gain of \$1,236,752. At December 31, 2013, \$14,265,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2014.
- \$15,880,000 was issued with an average interest rate of 3.153% to advance refund \$16,040,000 of outstanding 2005B bonds with an average interest rate of 4.740%. The net proceeds of \$18,157,485 (after payment of \$160,627 in bond issuance costs and \$319,888 debt service reserve fund) plus an additional \$374,706 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$27,328,875 from 2013 to 2035. The cash flow requirement on the new bonds is \$26,116,418 from 2013 through 2045. The advance refunding resulted in an economic gain of \$970,746. At December 31, 2013, \$16,040,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2015.
- \$15,955,000 was issued with an average interest rate of 3.584% to advance refund \$15,105,000 of outstanding 2005C bonds with an average interest rate of 4.857%. The net proceeds of \$17,131,175 (after payment of \$162,645 in bond issuance costs and \$441,689 debt service reserve fund) plus an additional \$358,234 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$30,928,656 from 2013 to 2045. The cash flow requirement on the new bonds is \$30,089,047 from 2013 through 2045. The advance refunding resulted in an economic gain of \$867,728. At December 31, 2013, \$15,105,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2015.

On May 9, 2012, the 2012B bonds were issued. The proceeds were used to refund portions of outstanding series 2003A, 2003B, and 2004B parity revenue bonds and funded the debt service reserve fund:

- \$29,220,000 was issued with an average interest rate of 3.353% to advance refund \$29,395,000 of outstanding bonds with an average interest rate of 4.914%. The net proceeds of \$ 31,450,816

## COLORADO SPRINGS UTILITIES

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(after payment of \$205,570 in bond issuance costs and \$648,714 debt service reserve fund) plus an additional \$719,274 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$55,000,870 from 2012 to 2033. The cash flow requirement on the new bonds is \$49,330,130 from 2012 through 2033. The advance refunding resulted in an economic gain of \$3,867,088. At December 31, 2012, \$29,395,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2013.

- \$36,370,000 was issued with an average interest rate of 2.194% to advance refund \$39,535,000 of outstanding bonds with an average interest rate of 4.757%. The net proceeds of \$43,901,486 (after payment of \$257,585 in bond issuance costs and \$528,058 debt service reserve fund) plus an additional \$942,369 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$57,327,838 from 2012 to 2025. The cash flow requirement on the new bonds is \$52,739,808 from 2012 through 2025. The advance refunding resulted in an economic gain of \$3,636,010. At December 31, 2012, \$39,535,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2014.
- \$42,425,000 was issued with an average interest rate of 3.585% to advance refund \$41,280,000 of outstanding bonds with an average interest rate of 4.941%. The net proceeds of \$44,144,352 (after payment of \$297,313 in bond issuance costs and \$1,130,889 debt service reserve fund) plus an additional \$1,002,518 of sinking fund monies were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered to be defeased and the liability for the old bonds has been removed from the Statements of Net Position. The cash flow requirement on the old bonds prior to the advance refunding was \$84,583,099 from 2012 to 2043. The cash flow requirement on the new bonds is \$77,482,553 from 2012 through 2043. The advance refunding resulted in an economic gain of \$4,729,128. At December 31, 2012, \$41,280,000 of bonds outstanding are considered defeased. The bonds are callable on November 15, 2013.

On September 26, 2012, the 2012C-1 bonds were issued. The proceeds refunded, along with other available monies, all of the outstanding utilities system subordinate lien refunding revenue bonds series 2002A and 2002B and funded the debt service reserve fund:

- \$113,565,000 was issued with an average interest rate of 2.576% to current refund \$130,260,000 of outstanding bonds with an average interest rate of 5.127%. The net proceeds of \$ 128,365,367 (after payment of \$611,471 in bond issuance costs and \$1,696,351 debt service reserve fund) plus an additional \$5,255,687 of sinking fund monies were used to prepay the outstanding debt service requirements on the old bonds. The cash flow requirement on the old bonds prior to the current refunding was \$201,186,108 from 2012 through 2030. The cash flow requirement on the new bonds is \$164,455,526 from 2013 through 2042. The current refunding resulted in an economic gain of \$27,553,548.

## COLORADO SPRINGS UTILITIES

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#### NOTE 8 - REVOLVING LOAN AGREEMENTS

Utilities entered into a Revolving Loan Agreement with U.S. Bank National Association (“U.S. Bank”) dated as of September 4, 2013 (the “2013 U.S. Bank Line of Credit”), and a Revolving Loan Agreement with KeyBank National Association (“KeyBank”) dated as of September 4, 2013 (the “2013 KeyBank Line of Credit”) together referred to as the “Credit Lines.” As of December 31, 2013, Utilities may receive advances up to \$25.0 million under the 2013 U.S. Bank Line of Credit, and \$50.0 million under the 2013 KeyBank Line of Credit, for a total of \$75.0 million to fund Utilities’ operating needs and normal expenditures including, without limitation, regularly scheduled capital expenses. Utilities’ repayment obligations under the Credit Lines are limited to the Net Pledged Revenues on a subordinate basis to the Parity Bonds and certain related obligations. The 2013 Credit Lines expire on September 4, 2016. Utilities has entered into several agreements similar to the Credit Lines over the past several years, and to date, Utilities has not drawn on any such agreement.

#### NOTE 9 - LONG-TERM LIABILITIES

##### *CHANGES IN LONG-TERM LIABILITIES*

Summary of changes in long-term liabilities as of December 31, 2013:

	Balance January 1, 2013	Additions	Reductions (in thousands)	Balance December 31, 2013	Current Portion
Revenue bonds	\$ 2,234,274	\$ 225,140	\$ 147,775	\$ 2,311,639	\$ 55,764
Issuance discounts and premiums	78,376	17,933	6,540	89,769	-
Total Bonds Payable	<u>2,312,650</u>	<u>243,073</u>	<u>154,315</u>	<u>2,401,408</u>	<u>55,764</u>
Other Long-term Liabilities					
Loans payable	19,678	-	1,511	18,167	1,531
Customer deposits	2,095	599	520	2,174	-
Compensated absences	13,038	16,252	16,000	13,290	7,536
Customer advances for construction	10,475	897	2,864	8,508	-
Municipal solid waste landfill closure and postclosure care	3,969	138	-	4,107	-
Derivative instruments	235,512	-	97,833	137,679	194
Other	2,005	781	129	2,657	-
Total Other Long-term Liabilities	<u>286,772</u>	<u>18,667</u>	<u>118,857</u>	<u>186,582</u>	<u>9,261</u>
Total Long-term Liabilities	<u>\$ 2,599,422</u>	<u>\$ 261,740</u>	<u>\$ 273,172</u>	<u>\$ 2,587,990</u>	<u>\$ 65,025</u>

Note: Immaterial differences may occur due to rounding.



## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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Summary of changes in long-term liabilities adjusted as of December 31, 2012:

	Balance January 1, 2012	Additions	Reductions (in thousands)	Balance December 31, 2012	Current Portion
Revenue bonds	\$ 2,203,208	\$ 315,685	\$ 284,619	\$ 2,234,274	\$ 50,774
Issuance discounts and premiums	49,575	37,554	8,753	78,376	-
Total Bonds Payable	<u>2,252,783</u>	<u>353,239</u>	<u>293,372</u>	<u>2,312,650</u>	<u>50,774</u>
Other Long-term Liabilities					
Loans payable	21,089	-	1,411	19,678	1,511
Customer deposits	1,995	734	634	2,095	-
Compensated absences	12,595	16,313	15,870	13,038	7,474
Customer advances for construction	10,330	450	305	10,475	-
Municipal solid waste landfill closure and postclosure care	3,874	262	167	3,969	-
Derivative instruments	283,190	-	47,678	235,512	12,326
Other	1,810	325	130	2,005	129
Total Other Long-term Liabilities	<u>334,883</u>	<u>18,084</u>	<u>66,195</u>	<u>286,772</u>	<u>21,440</u>
Total Long-term Liabilities	<u>\$ 2,587,666</u>	<u>\$ 371,323</u>	<u>\$ 359,567</u>	<u>\$ 2,599,422</u>	<u>\$ 72,214</u>

Note: Immaterial differences may occur due to rounding.

### **INTEREST COST, EXPENSE AND PAYMENTS**

Interest cost to interest expense reconciliation for year ended December 31:

	2013	2012
	(in thousands)	
Total interest cost	\$ 102,284	\$ 102,972
Interest directly capitalized on SDS	(10,980)	(9,051)
Capital interest component	(6,422)	(3,455)
Amortization of discounts, (premiums) and deferred (gain) loss on refundings	(3,413)	(1,594)
Total Interest Expense	<u>\$ 81,469</u>	<u>\$ 88,872</u>

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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Interest cost to interest payments reconciliation for year ended December 31:

	2013	2012
	(in thousands)	
Total interest cost	\$ 102,284	\$ 102,972
Accrued interest December 31 of current year	(12,572)	(12,189)
Accrued interest December 31 of prior year	12,189	13,658
Total Interest Payments	<u>\$ 101,901</u>	<u>\$ 104,441</u>

Note: Immaterial differences may occur due to rounding.

#### NOTE 10 - MUNICIPAL SOLID WASTE LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS

Utilities is subject to the Colorado Department of Public Health and Environment regulations which require Utilities to incur closure and postclosure care costs for landfills. In 2013 and 2012, Utilities recognized a liability of \$4,106,994 and \$3,969,474, respectively, for closure and postclosure care costs based upon landfill capacity used to date. The estimated total current cost of closure and postclosure care to be recognized for Utilities' landfills is \$7,563,652 and \$7,473,965, respectively. The average landfill capacity used to date in 2013 and 2012 is 63.1% and 61.7%, respectively. The estimated remaining landfill lives vary from 18 to 88 years. There are no financial assurance requirements or restricted assets for the payment of closure and postclosure care costs. Estimates of closure and postclosure costs are stated in current dollars and shall be adjusted annually for inflation and changes in laws and regulations. The last independent assessment was performed in 2012.

#### NOTE 11 - DEFINED BENEFIT PENSION PLAN

Utilities contributes to the Local Government Division Trust Fund, a cost-sharing, multiple-employer defined benefit pension plan ("Plan") administered by the Public Employees' Retirement Association of Colorado ("PERA"). The Plan provides retirement and disability, annual increases, and death benefits for members or their beneficiaries. All permanent employees are Plan members. Title 24, Article 51 of the Colorado Revised Statutes ("CRS"), as amended, assigns the authority to establish benefit provisions to the Colorado State Legislature. PERA issues a publicly available annual financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained online at [www.copera.org](http://www.copera.org) or by writing to Colorado PERA, 1301 Pennsylvania Street, Denver, Colorado 80203, or by calling PERA at (303) 832-9550 or 1 (800) 759-PERA (7372).

Plan members and Utilities are required to contribute to the Plan at a rate set by statute. The contribution requirements of Plan members and Utilities are established under Title 24, Article 51, Part 4 of the CRS, as amended. The statutory employer contribution rate in 2013 and 2012 is 8.0% of covered salary for plan members and 10.0% of covered salary for Utilities. A portion of Utilities' contribution (1.02% of covered salary) is allocated for the Health Care Trust Fund (see Note 13, Postemployment Health Care and Life Insurance Benefit - Multiple-Employer). Beginning January 1, 2010, Utilities was required to pay an amortization equalization disbursement equal to 2.2% and supplemental amortization equalization disbursement equal to 1.5% of the total payroll which is included in the total contribution rate of 13.7% of covered salary. Utilities contributions to the Plan for the years ending December 31, 2013, 2012 and 2011, were \$18,701,657, \$18,552,419, and \$18,034,840, respectively, equal to their required contributions for each year.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

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#### **NOTE 12 - DEFINED CONTRIBUTION PENSION PLAN**

##### ***401(k) PLAN***

Employees of Utilities may voluntarily contribute to the Voluntary Investment Program ("401(k) Plan"), an Internal Revenue Code section 401(k) defined contribution plan administered by PERA. Contributions are separate from others made to PERA. Title 24, Article 51, Part 14 of the CRS, as amended, assigns the authority to establish the 401(k) Plan provisions to the Colorado State Legislature.

The 401(k) Plan is funded by voluntary member contributions up to a maximum limit set by the IRS (\$17,500 in 2013, \$17,000 in 2012, \$16,500 in 2011 or 100% of salary, whichever is less). There is a catch-up provision that allows participants 50 years of age and older who are contributing the maximum to contribute an additional \$5,500 annually to their account. The 401(k) Plan member contributions from Utilities for the years ending December 31, 2013, 2012 and 2011, were \$3,304,500, \$3,252,269 and \$3,300,362, respectively.

##### ***INTERNATIONAL CITY/COUNTY MANAGEMENT ASSOCIATION ("ICMA") 401(a) PLAN***

Utilities provides, by authority of a City Council Resolution, an ICMA 401(a) Plan, a defined contribution plan, administered by ICMA Retirement Corporation, which defines eligibility and participation requirements. Employer contributions from Utilities for the years ending December 31, 2013, 2012 and 2011 were \$13,289, \$13,289 and \$13,956, respectively.

#### **NOTE 13 - POSTEMPLOYMENT HEALTH CARE AND LIFE INSURANCE BENEFIT**

##### ***MULTIPLE-EMPLOYER***

Utilities contributes to the Health Care Trust Fund ("HCTF"), a cost-sharing, multiple-employer postemployment health care plan administered by PERA. The HCTF provides a health care premium subsidy to PERA participating benefit recipients and their eligible beneficiaries. Title 24, Article 51, part 12 of the CRS, as amended, assigns the authority to establish the HCTF benefit provisions to the Colorado State Legislature. PERA issues a publicly available annual financial report that includes financial statements and required supplementary information for the HCTF. That report may be obtained online at [www.copera.org](http://www.copera.org) or by writing to Colorado PERA, 1301 Pennsylvania Street, Denver, Colorado 80203, or by calling PERA at (303) 832-9550 or 1 (800) 759-PERA (7372).

Utilities is required to contribute at a rate of 1.02% of covered salary for all PERA members as set by statute and included in the statutory employer contribution rate of 10.0% of covered salary (see Note 11, Defined Benefit Pension Plan). No member contributions are required. The contribution requirements for Utilities are established under Title 24, Article 51, Part 4 of the CRS, as amended. The apportionment of the contribution to the HCTF is established under Title 24, Article 51, Section 208 of the CRS, as amended. Utilities' contributions to HCTF for the years ended December 31, 2013, 2012 and 2011 were \$1,392,386, \$1,381,275 and \$1,342,790, respectively, equal to their required contributions for each year.

##### ***SINGLE-EMPLOYER***

In accordance with the City Code, Utilities offers a health care plan to retirees with Utilities' contribution determined by City Council. Employees eligible to retire prior to January 1, 1979, receive this health care plan without cost to the employee. Those eligible to retire after January 1, 1979 and hired prior to August 1, 1988 receive a limited Utilities' contribution not to exceed \$91.40 per month. During 2013, these benefits were provided to 1,121 retired employees at a cost of \$1,277,278. Of the 1,121 retirees, 24 were retirees with full coverage and 1,097 were retirees with partial coverage. The partial coverage payments totaled \$1,202,641 and full coverage payments totaled \$74,637. During 2012, these benefits were provided to 1,112 retired employees at a cost of \$1,264,738. Of the 1,112 retirees, 28 were retirees with

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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full coverage and 1,084 were retirees with partial coverage. The partial coverage payments totaled \$1,189,296 and full coverage payments totaled \$75,442.

All employees hired after August 1, 1988, receive no contribution from Utilities for this health care plan. In addition to regular medical insurance subsidies, Utilities also funds a Medicare supplement for eligible retirees. In 2013, Utilities paid a total of \$31,768 to 24 retirees. Retiree life insurance premiums were paid on behalf of 1,157 retirees for a total cost in 2013 of \$5,480. All amounts paid are equal to required contributions. In 2012, Utilities paid a total of \$32,967 to 26 retirees. Retiree life insurance premiums were paid on behalf of 1,179 retirees for a total cost in 2012 of \$6,531. All amounts paid are equal to required contributions.

Post-retirement health care and life insurance benefits are considered to be an unfunded plan since there are no dedicated assets and retiree benefits are paid annually in an amount equal to the benefits distributed or claimed in that year (pay-as-you-go basis).

**Annual OPEB Cost and Net OPEB Obligation** - Utilities' annual Other Post-Employment Benefit ("OPEB") cost (expense) is calculated based on the Annual Required Contribution ("ARC") to the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Annual OPEB cost for 2013 and 2012 and Net OPEB obligation as of December 31:

	2013	2012
	(in thousands)	
OPEB Obligation:		
Annual Required Contribution	\$ 1,555	\$ 1,603
Interest on Net OPEB Obligation	60	48
Adjustment to Annual Required Contribution	(79)	(85)
Annual OPEB cost	1,536	1,566
Contributions made	(1,315)	(1,297)
Increase in Net OPEB Obligation	221	269
Net OPEB Obligation, January 1	1,337	1,068
Net OPEB Obligation, December 31	\$ 1,558	\$ 1,337

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

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Utilities' annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the Net OPEB obligation for 2013, 2012 and 2011:

Year	Annual OPEB Cost (in thousands)	% of Annual OPEB Cost Contributed	Net OPEB Obligation
2013	\$ 1,536	85.6%	\$ 1,558
2012	1,566	82.8%	1,337
2011	1,586	82.7%	1,068

Note: Immaterial differences may occur due to rounding.

**Actuarial Methods and Assumptions** - Projections of benefits for financial reporting purposes are based on Utilities' post-retirement benefit plan as of January 1, 2013. The retiree benefits included in the actuarial valuation are the medical benefits offered to a closed group of retirees and the life benefits offered to a closed group of retirees who retired by December 31, 2012. The types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members are based on a point in time. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2013 actuarial valuation, the projected unit credit method was used. The actuarial assumptions included a 4.5% annual discount rate based on the expected rate of return for investments on employer assets, which generally consist of short-term liquid investments. The unfunded actuarial accrued liability ("UAAL") is amortized over the maximum acceptable period of 30 years for the life benefit and average remaining lifetime of retirees (17 years) for the medical benefit, on an open basis. The amortization is calculated assuming a level percentage of projected payrolls. The cost trend rate applied on a select and ultimate basis was 8.0% and 5.0%, respectively.

**Funding Status and Funding Progress** - The funded status of the plan as of January 1, 2013, the most recent actuarial valuation date, was as follows:

	January 1, 2013 (in thousands)
OPEB Obligation:	
Actuarial accrued liability	\$ 18,000
Actuarial value of plan assets	-
Unfunded Actuarial Accrued Liability	<u>\$ 18,000</u>
Funded ratio	0.0%
Covered payroll (active plan members)	\$ 1,555
Unfunded Actuarial Accrued Liability as a percentage of covered payroll	1157.6%

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

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Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the Notes, present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Between 2013 and 2011, assumptions used in the actuary study in aggregate accounted for the difference in the Actuarial Accrued Liability (“AAL”) decrease.

Schedule of funding progress (Unaudited):

Actuarial Valuation Date	Actuarial Value of Assets	AAL	UAAL (in thousands)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
1/1/13	\$ -	\$ 18,000	\$ 18,000	0.0%	\$ 1,555	1157.6%
1/1/11	-	18,602	18,602	0.0%	1,615	1151.8%
1/1/09	-	17,074	17,074	0.0%	1,549	1102.3%

Note: Immaterial differences may occur due to rounding.

#### **NOTE 14 - COMMITMENTS**

Under Article 7-60 of the City Charter, the City cannot enter into agreements involving the expenditure of public funds (with certain limited exceptions) unless funds have been appropriated by the City Council to liquidate the liability created by the agreement. In accordance with this City Charter provision, each of Utilities’ agreements (with certain limited exceptions) contains clauses that, in general, terminate the agreement without further liability to Utilities if funds are not appropriated by the City Council (in whole or in part) that are sufficient to perform Utilities’ obligations under the agreement. Such an agreement clause is referred to as an “appropriations clause.”

#### **CONSTRUCTION COMMITMENTS**

Construction commitment amounts represent contract price less payments applied on outstanding retainage construction contracts. Utilities’ total construction and commitments as of December 31, 2013 and 2012 were \$251,386,611 and \$80,730,397, respectively.

#### **ELECTRIC COMMITMENTS**

**Electric Generation Fuel Supply Agreements** - Utilities’ hydro and coal units are normally operated as base-load facilities. Utilities’ coal supplies and transportation services are procured through a portfolio of contracts which are managed to ensure a dependable fuel supply. Demand for coal has fallen from the prior year as natural gas continues to replace coal as a more economic generation fuel. Term coal supply contracts are currently believed to be at or above the commodity market prices. Spot market coal is purchased to supplement term contract volumes as needed.

## COLORADO SPRINGS UTILITIES

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**Electric Power Purchase Agreements** - Utilities has electric power purchase agreements with other power producers to purchase capacity and associated energy to supplement existing generation resources. The agreements have various terms and conditions. Utilities' largest purchase power contract is with Western Area Power Administration. In addition to the purchase power agreements that supplement existing generation, Utilities has a wind power purchase agreement to add to Utilities' green energy portfolio in effect through December 31, 2014.

**Contractual Service Agreement** - Utilities has a contractual service agreement with General Electric International, Inc. ("GE"). This contractual service agreement was amended on December 21, 2012 and requires that GE perform all major maintenance activities on the two GE combustion turbines through an estimated 138,000 run hours. The total run hours are estimated to be achieved in the fourth quarter 2026.

**Total Electric Commitments** - As of December 31, 2013, the approximate minimum obligations, subject to any appropriations clauses, for these Electric Commitments over the next five years are:

<u>December 31,</u>	<u>Amount</u>
	(in thousands)
2014	\$ 41,065
2015	36,804
2016	32,316
2017	18,943
2018	18,864

### NATURAL GAS COMMITMENTS

**Natural Gas Supply and Transport Agreement** - Utilities contracts for sufficient firm transportation capacity and supplies to meet its firm sales customers' peak day needs and fuel gas requirements for power generation. Utilities defines peak day conditions as a day with an average temperature of -13 degrees Fahrenheit. Utilities' goal is to hold a diversified portfolio of natural gas supplies, pipeline transportation and storage services in order to provide reliability and economic efficiency in meeting supply obligations.

Utilities' firm natural gas supply portfolio is comprised of multiple contracts with terms ranging from three months to thirty years. The expiring contracts are competitively bid by the suppliers each year, usually during the spring. In addition, Utilities purchases approximately 20.0% of its annual natural gas supply needs on a short-term (30-day or less) basis, giving Utilities the flexibility to react to warmer than normal conditions without defaulting on firm commitments and providing the flexibility to take advantage of short-term drops in natural gas prices. The staggered terms of the supply contracts help shape supply commitments to better match load requirements, and ensure Utilities can acquire and replace supplies in an orderly fashion.

In addition to a diversified portfolio within the context of terms and conditions of service, Utilities actively pursues opportunities to reduce costs and realize value from its natural gas supply assets. This process includes releasing transportation and storage capacity to meet peak loads during non-peak periods and other asset optimization strategies to capture value from any available asset capacity.

**Natural Gas Price Hedge Program** - Utilities' Energy Risk Management Policy strives to reduce price uncertainty and, thereby, allows customers to plan and budget for their utilization of utility services. In order to limit and manage Utilities' exposure to price uncertainty, a long standing natural gas hedging program required specific volumes to be hedged according to a defined schedule. Utilities hedged its

## COLORADO SPRINGS UTILITIES

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natural gas supplies for both retail natural gas customers and its fuel gas for power generation. This hedging program successfully reduced price uncertainty through periods of high natural gas price volatility. Natural gas hedging activities for 2014 and beyond have been suspended pending results of an ongoing program evaluation. No natural gas hedges are in effect for calendar year 2014 and beyond. The suspension in hedging activities is under continual evaluation and may only be resumed with the approval of Utilities' Risk Management Committee and Utilities Board.

**Total Natural Gas Commitments** - As of December 31, 2013, the approximate minimum obligations, subject to any appropriations clauses, for these Natural Gas Commitments over the next five years are:

<u>December 31,</u>	<u>Amount</u>
	(in thousands)
2014	\$ 73,462
2015	35,205
2016	25,222
2017	17,812
2018	13,936

#### **NATURAL GAS PREPAY AGREEMENT**

On June 27, 2008, The City (on behalf of Utilities) entered into a Natural Gas Supply Agreement ("Supply Agreement") with Public Authority for Colorado Energy ("PACE"), a component unit of the City, for financial reporting purposes. The Supply Agreement will continue in effect until September 30, 2038, unless terminated earlier due to certain defaults, as set forth therein, or the termination of PACE's Prepaid Gas Agreement. The City is obligated to purchase and pay for natural gas tendered for delivery by PACE at an index minus a predetermined discount. If PACE fails on any day, for any reason other than Force Majeure, to deliver the quantity of natural gas required to be delivered pursuant to the Supply Agreement, the City will have no obligation for any of the natural gas supply that was not delivered as a result of such PACE delivery default.

Certain risk exists that all or part of the discount associated with this gas prepay transaction will not be realized as a result of the financial creditworthiness of the counterparties to agreements associated with the transaction and the potential failure of such counterparties to fulfill their contractual obligations, including financial remedies. As of December 31, 2013, all of the counterparties to agreements associated with the gas prepay transaction are fulfilling their contractual obligations.



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#### **WATER COMMITMENTS**

**Water Storage Agreements** - Utilities contracts with the Bureau of Reclamation for water storage in Pueblo Reservoir for SDS. The Bureau of Reclamation will provide reimbursement for costs associated with the construction and connection of the pipe onto the Pueblo Reservoir Dam. The reimbursement will be netted against storage commitment bills through 2017. The contract expires December 31, 2049, unless extended or terminated earlier in accordance with the provisions of the contract.

**Total Water Commitments** - As of December 31, 2013, the approximate minimum obligations with the approximate reimbursements for this Water Commitment over the next five years are:

December 31,	Commitment Amount	Reimbursement Amount (in thousands)	Commitment Net Amount
2014	\$ 702	\$ 701	\$ 1
2015	734	733	1
2016	767	766	1
2017	801	311	490
2018	836	-	836

#### **NOTE 15 - CONTINGENCIES AND CLAIMS**

##### **ENVIRONMENTAL MATTERS**

Numerous federal, state and local environmental laws and regulations affect Utilities' facilities and operations. Utilities monitors its compliance with environmental laws and regulations on an ongoing basis.

**Air Quality** - In operating the Electric System, Utilities is subject to environmental requirements, which affect operating and capital costs of the System. Ongoing promulgation of new regulations under the Clean Air Act Amendments of 1990 and the Colorado Air Quality Control Act will have the effect of imposing more stringent air emission requirements for the Electric System's generating facilities, particularly the Nixon and Drake coal-fired units.

Drake Units 5, 6 and 7 (all coal-fired), Nixon Units 1 (coal-fired), 2 and 3 (both gas-fired), and Front Range Power Plant Units 1 and 2 (both gas-fired) are subject to the Clean Air Act Title IV Phase 2 Acid Rain Requirements. Utilities has sufficient emission allowances that it believes will satisfy its sulfur dioxide ("SO<sub>2</sub>") allowance obligations into 2018. Thereafter, Utilities expects to have pollution control technology in operation to remain in compliance with the sulfur dioxide requirements for these units.

The Federal Clean Air Act requires that states develop "State Implementation Plans" ("SIPs") that address how each state will control air pollution, including visibility impacts to Class I federal areas. The Environmental Protection Agency's ("EPA") Regional Haze Rule requires that certain emission sources, such as power plants that may reasonably be anticipated to cause or contribute to visibility impairment in Class I areas to install Best Available Retrofit Technology ("BART"). The BART emission limits for nitrogen oxides ("NO<sub>x</sub>") for Drake will be met by the installation of over fire air and ultra low NO<sub>x</sub> burners on Units 5, 6, and 7. The BART emission limits for SO<sub>2</sub> for Drake will be met by scrubbers for Units 6 and 7 and dry sorbent injection for unit 5. The estimated remaining cost of these controls is \$104.0 million. These controls must achieve compliance with emission limits no later than January 30, 2018.

## COLORADO SPRINGS UTILITIES

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Additionally, Colorado's Regional Haze SIP phases in emission limits for other stationary sources, such as Nixon, as part of "Reasonable Progress" towards natural levels of visibility under the Regional Haze Rule. The Reasonable Progress emission limits for NOx for Nixon will be met by the installation of over fire air and ultra low-NOx burners and the Reasonable Progress emission limits for SO2 will be met by the installation of a scrubber. The estimated remaining cost of these controls is \$101.0 million. These controls must achieve compliance with the emission limits by December 31, 2017.

For particulate matter control, both Nixon and Drake have been equipped with fabric filter baghouses. Currently these baghouses achieve a removal efficiency of greater than 95%. Through its BART and Reasonable Progress analysis of Drake and Nixon, the State has determined that the existing baghouses represent the most stringent controls for particulate matter and will be sufficient to meet BART and Reasonable Progress limits.

The Regional Haze Rules requirements for Drake and Nixon were approved by the State legislature in May 2011. The EPA approval of the SIP had an effective date of January 30, 2013. Utilities submitted its required proposed Compliance Schedule to the Air Pollution Control Division ("APCD") of the Colorado Department of Public Health and Environment ("CDPHE") on March 28, 2013. The proposed compliance schedule was reviewed by the APCD and noticed to the public on June 17, 2013 for a 30-day comment period ending July 17, 2013. On August 21, 2013, Utilities submitted a proposed revision to its compliance schedule, which was again noticed to the public for a 30-day period ending October 4, 2013. On November 4, 2013, Utilities was notified by the APCD that the compliance schedule proposed by Utilities was approved.

Additional regulations, such as the ongoing review of the federal ozone standard, may necessitate the installation of additional pollution controls beyond those described above. While it is uncertain the extent to which these regulations will affect Utilities' power plants or operations, additional future pollution controls for NOx, i.e., post-combustion controls such as Selective Catalytic Reduction, could potentially cost Utilities an additional \$100.0 million to \$150.0 million within the next ten years.

With regard to the EPA's final Maximum Achievable Control Technology rule, finalized in December 2011 as the Mercury and Air Toxics Standard, emissions testing performed in recent years indicate that Utilities is in compliance with the limits in the Mercury and Air Toxics Standard for all of the Nixon and Drake coal-fired boilers. It is expected that the combination of planned scrubbers and existing baghouses will also be adequate to meet these new standards. While additional monitoring, testing and reporting will be required (i.e., installation of continuous emissions monitoring systems for mercury) capital investment is estimated to be less than \$1.0 million for all coal-fired units combined.

In May 2010, the EPA issued its final "Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule" for regulating greenhouse gas emissions, and the rule has been adopted by Colorado. New construction projects that emit at least 100,000 tons of greenhouse gases and existing facilities that increase their emissions by at least 75,000 tons per year must obtain a construction permit even if they do not exceed thresholds for other pollutants. New and upgraded facilities that are subject to the requirements will be required to install BART to control their greenhouse gas emissions. Utilities routinely evaluates the impact of Prevention of Significant Deterioration regulations on proposed projects and, at this time, there are no planned projects which would be subject to increased cost or operational restrictions as a result of the greenhouse gas Prevention of Significant Deterioration regulations. On June 25, 2013, President Obama directed EPA to develop carbon pollution standards for new and existing power plants. Proposed standards for new plants are expected to be finalized after 2013, while proposed standards for existing plants are expected to be finalized by the end of 2015. At this time, the future capital costs of compliance with these future greenhouse gas regulations cannot be estimated. Utilities

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reports its greenhouse gas emissions under new EPA reporting regulations and voluntarily through the Climate Registry.

In June 2010, the EPA issued a proposed rule regarding “Coal Combustion Residuals” (“CCRs”), which are also referred to as “coal combustion byproducts” or “coal ash”. The proposed rule considered two approaches for disposal of CCRs, one to regulate CCRs under subtitle C of the Resource Conservation and Recovery Act as a special waste and the second under subtitle D of the Resource Conservation and Recovery Act as a non-hazardous waste. Either approach will increase costs to Utilities for the ongoing disposal of these materials. The most significant increase would result from CCRs being regulated under subtitle C. It is estimated that this scenario could increase Utilities’ annual disposal costs from \$1.0 million to \$10.0 million. It is anticipated that the EPA will establish a final rule with regards to disposal of CCRs in 2014. Utilities currently disposes of its CCRs at its Clear Spring Ranch Solids Handling and Disposal facility under a County solid waste disposal authorization known as a “Certificate of Designation.”

In February 2012, the CDPHE adopted revisions to Section 9 (regarding waste impoundments) of its “Regulations Pertaining to Solid Waste Sites and Facilities.” Additional capital investment in the range of \$1.0 million to \$9.0 million for existing impoundments at Drake and Nixon may be required to meet these revisions in the 2015-2017 timeframe. Utilities expects to receive clarity from the CDPHE in 2014 regarding the extent for impoundment related capital investment following their review of Utilities’ preliminary impoundment classification submittals. The revised regulation will require both plants to obtain a “Certificate of Designation” from both the City and El Paso County and require that financial assurance be maintained for any future closure of these impoundments. Demonstration of adequate financial assurance will likely be required in 2014.

In June 2013, the EPA proposed Effluent Limit Guidelines for electric power generating stations. EPA proposed eight regulatory options and identified a middle option as its preferred alternative. Nixon is a zero discharge facility and is unlikely to be affected by the final version of the rule, regardless of the alternative selected. Some of the EPA’s most stringent proposals could result in additional capital expenditures for improvements to Drake. The probability and extent of such costs is being assessed by Utilities. The proposed rule contemplates a compliance period between 2017 and 2022.

**Wastewater Quality** - Utilities operates the Las Vegas Street Wastewater Treatment Plant, which discharges treated wastewater to Fountain Creek, and the J.D. Phillips Water Reclamation Facility, which discharges treated wastewater to Monument Creek. Both facilities operate under the terms of Colorado Discharge Permit System (“CDPS”) permits issued in 2006 pursuant to the Federal Clean Water Act. Under the CDPS permits, Utilities is required to monitor wastewater discharges and report on a monthly basis the results of that monitoring to the CDPHE. In 2010, permit renewal applications were submitted to the CDPHE as required for both facilities. The permits are expected to be renewed in 2014. Utilities continues to operate under administrative extension of the existing permits until such time that renewed permits are issued.

In accordance with the CDPHE regulations, Utilities is subject to public health protection limits for E. coli and turbidity applicable to the distribution system for reclaimed wastewater used for nonpotable purposes. Utilities does not expect that additional capital or other expenditures will be required to comply with these regulations in the next several years.

The CDPS permits for the facilities require that when peak monthly throughput and treatment reach 80.0% of facility design capacity, Utilities must initiate engineering and financial planning for additional treatment capacity, and that construction must be commenced when peak monthly throughput and treatment is at 95.0% capacity. For both facilities, the throughput and treatment are currently below these capacity standards. Peak monthly organic treatment and hydraulic throughputs in 2013 for the Las Vegas

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Street Wastewater Treatment Plant reached 44.5% and 44.9% of the respective capacities. Peak monthly organic treatment and hydraulic throughputs in 2013 for the J.D. Phillips Water Reclamation Facility reached 45.8% and 39.9% of the respective capacities.

Utilities is actively engaged in the State's water quality regulatory rulemaking processes. A new ultraviolet disinfection system for the Las Vegas Street Wastewater Treatment Plant came on-line in January 2011 to both enable the facility to meet more stringent future E. coli limits as well as reduce operational and regulatory risks associated with chlorine gas disinfection. The CDPHE changed Fountain and Monument Creeks' stream designations from "use-protected" to "reviewable" in July 2008. Utilities expects to see the first impact of this change in the discharge permit renewal negotiations anticipated in 2014. This change may ultimately result in more stringent effluent limits for pollutants that have been detected in the discharge but are not limited by the treatment facilities' current CDPS permits. Additionally, pollutants that are currently limited by the CDPS permits may undergo an "antidegradation" review that could result in more restrictive effluent limits. Reduced or additional permitted effluent limits may necessitate additional wastewater treatment facility controls.

The CDPHE adopted regulations for reducing nutrients (nitrogen and phosphorus) in state waters through 2022 which became effective in September 2012. Additional capital investment will be required to meet these standards. Based on these regulations, approximately \$3.1 million in capital investment will be required at the Las Vegas Street Wastewater Treatment Plant between 2014 and 2022. In July 2013, Utilities was awarded a \$1.0 million construction grant from the State's Nutrient Grant Program to offset these costs. Current plans are for design in 2015 with construction of plant upgrades in 2016 and 2017. The J.D. Phillips Water Reclamation Facility will be able to meet the proposed standards with a \$1.5 million process improvement project currently in design and planned for construction in 2014. However, some nutrient regulatory scenarios could result in much greater capital investment being required after 2022.

As required by discharge permits, Utilities has reported both sanitary sewer overflows ("SSOs") and reclaimed wastewater releases to regulatory agencies. SSOs can be caused by blockages in the sewer lines due to debris, tree roots and grease or can be caused by vandalism, construction damage, pump or pipeline failures and severe flooding. In 2004, the CDPHE and Utilities entered into a Compliance Order on Consent ("Consent Order") which addresses capacity and condition evaluations, along with the systematic repair, rehabilitation and replacement of portions of the wastewater collection system through the year 2012. The Consent Order was reviewed and approved by the EPA. The Consent Order was subsequently amended in 2005, 2006 and 2010 to resolve SSOs that occurred through December 2009. On January 29, 2013, Utilities submitted a "Notice of Completion" to the CDPHE for the Consent Order and subsequent amendments. In a letter dated March 8, 2013, the CDPHE informed Utilities that the Notice of Completion ". . . was satisfactory and Colorado Springs has fully responded to and met its obligations pursuant to the Consent Order." As a result, the CDPHE formally closed the Consent Order and no further action is required from Utilities on this matter.

The Clear Spring Ranch Solids Handling and Disposal Facility, which processes sludge from the Las Vegas Street Wastewater Treatment Plant and the J.D. Phillips Water Reclamation Facility, is currently regulated under a federal sludge disposal permit, the CDPHE's solid waste regulations, a County solid waste disposal authorization known as a "Certificate of Designation" and State air quality permits. Under these permits and related regulations, Utilities is required to frequently monitor sludge and ground water quality. In May 2013, the EPA reauthorized the general permit for sludge disposal which expires on May 15, 2018. Utilities was notified by EPA on July 30, 2013 that it is now covered under this reauthorized permit. The solid waste disposal Certificate of Designation has no expiration date.

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In February 2012, the CDPHE adopted revisions to Section 9 (regarding waste impoundments) of its "Regulations Pertaining to Solid Waste Sites and Facilities." Additional capital investment in the range of \$7.0 million to \$15.0 million for existing impoundments at the Clear Spring Ranch Solids Handling and Disposal Facility may be required to meet these revisions in the 2015-2017 timeframe. Utilities expects to receive clarity from the CDPHE in 2014 regarding the extent for impoundment-related capital investment following their review of Utilities' preliminary impoundment classification submittals. The revisions may require that the site's Certificate of Designation be amended and will require that financial assurance be maintained for any future closure of the impoundments.

In 2009, a "Wastewater Integrated Master Plan" was drafted and internally reviewed. This plan addresses the 10-year capital improvement projects needed for the wastewater collection system, wastewater treatment facilities and Clear Spring Ranch Solids Handling and Disposal Facility. It analyzes current capacity and future growth needs for wastewater system components. The plan also addresses the impacts of new regulations and plans for capital improvements necessary to keep the facilities in compliance with the new regulations.

**Drinking Water Quality** - The Federal Safe Drinking Water Act, originally passed in 1974 and amended in 1986 and 1996, is enforced by federal and state agencies with responsibility over drinking water protection. The law requires actions by public water systems to protect drinking water from the source (e.g., rivers, reservoirs and groundwater wells) to the customer's tap. This regulatory oversight applies to the public water systems' storage, treatment and distribution facilities, as well as operational practices.

The Federal Safe Drinking Water Act authorizes the EPA to establish national health-based standards for the protection of drinking water from both naturally occurring and man-made contaminants. Additionally, the EPA maintains a list of unregulated contaminants that are not currently subject to any proposed or promulgated national primary drinking water regulation, but that are known or anticipated to occur in public water systems and may become subject to regulation in the future. As such, there is always the potential for new and/or more stringent standards that may impose additional costs to Utilities, either to existing infrastructure or operations or to new water project development. Utilities' current long-term capital improvements forecast for the Water System addresses normal repairs and replacements in the treatment and distribution facilities to maintain both operational reliability and compliance with the Federal Safe Drinking Water Act and applicable regulations. Utilities is required to provide a sufficient capacity and level of water treatment and disinfection necessary to meet EPA-established "maximum contaminant levels" for regulated contaminants as well as provide regular monitoring for these contaminants in its treatment plants and distribution systems. Utilities' laboratory performs chemical, physical and biological analyses of its finished water supplies, and is certified by the CDPHE for the analysis of drinking water. The CDPHE and the EPA have the authority to enforce drinking water quality standards for the water supplied by the Water System. The CDPHE periodically conducts compliance inspections of the water treatment processes and laboratory monitoring provided by Utilities. The laboratory is capable of meeting future analytical demands in response to system capacity additions and increased regulatory requirements. As part of the "consumer awareness" provisions of the Federal Safe Drinking Water Act, Utilities is required to submit annual "consumer confidence reports" to its customers addressing the sources of its drinking water and the levels of regulated contaminants found in the drinking water through its monitoring programs. Utilities' annual Water Quality Report to its customers consistently notes that the water treated and supplied by Utilities meets applicable primary drinking water quality standards. Other provisions of the Federal Safe Drinking Water Act require Utilities to maintain operator certifications, submit a Source Water Assessment report to the CDPHE, and maintain a cross-connection program.

**Water Supply** - Federal and state legislation often influences Utilities' water development activities. Such legislation and regulations promulgated by federal and state agencies generally implement environmental policies concerned with land use, appropriation and allocation of water resources and water quality. The

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constraints imposed by environmental laws and regulations could potentially limit Utilities' current system yield or further expansion of existing water projects (particularly transmountain projects) as well as prohibit new project development. The following discussion summarizes some of the issues raised by existing laws and regulations.

The National Environmental Policy Act of 1969 requires the review of any project that includes a major federal action (usually the issuance of permits by federal agencies) to determine if the project will cause significant impacts on the environment, and if so to require appropriate mitigation measures. As part of this environmental assessment process, reasonable alternatives to the proposed project must also be evaluated and reviewed as part of the federal decision-making process. This requirement has had the effect of both delaying projects and increasing project costs.

The Federal Land Policy and Management Act authorizes the federal government to grant easements or issue special use permits for rights-of-way for water facilities crossing or located upon federal property. The Federal Land Policy and Management Act requires that special use permits include conditions necessary to protect the environment. All rights-of-way issued under the Federal Land Policy and Management Act are for a limited period of time and frequently contain reopener provisions. Upon renewal or reopening of the various special use permits that Utilities currently holds for the Water System, additional conditions, such as minimum stream flows or bypass requirements, might be imposed that could reduce the yield of related parts of the Water System in the future.

The federal government has designated large parcels of federally owned mountain land as controlled land use areas pending an evaluation for possible inclusion within the national wilderness preservation system. The inclusion of land within a wilderness area can render a water source unusable due to access restrictions and federal reserved water rights claims, or force a change to a less desirable, more expensive alternative development or operation plan.

The United States Forest Service is pursuing, or may pursue in the future, legal action in which it claims vested federal reserved water rights to water flowing in and through National Forests and other federally owned lands. Some of these claimed federal reserved water rights are or would be superior to some of the water rights owned by the City within Colorado's water allocation system. The areas of primary concern to the City are the Arapaho and White River National Forests, both of which were reserved in 1905. These forests, located within the Colorado River and Arkansas River drainages, encompass the sources of the City-owned rights and entitlements connected with the Homestake Project, the Blue River Project, the Twin Lakes Project and the Fryingpan-Arkansas Project.

The Federal Wild and Scenic Rivers Act is designed to protect certain free-flowing rivers identified by federal agencies. This Act authorizes Congress to designate segments of a river as wild, scenic, or recreational depending upon the presence of valued characteristics, such as recreational access, and other detracting factors, such as the degree of existing encroachment. Designation of a segment requires federal agencies to manage the river and adjacent lands to protect the identified valued characteristics and provides legal support for the appropriation of a new federal water rights. Both of these effects present potential issues that could restrict the operations and development of the Water System.

The Federal Clean Water Act, as amended in 1987 and currently enforced by federal and state entities with responsibility over water quality protection, creates some potential for additional constraints on water operations and development activities. For example, in a United States Supreme Court case the Court considered hydrologic modifications as "pollution" under the Federal Clean Water Act, and stated that instream flow requirements as special use permit conditions may be appropriate to protect designated stream uses. Similarly, recent federal courts of appeals decisions (outside Utilities' jurisdiction) raise the issue of whether a permit is necessary to transfer raw water from one water body to another. Such

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conditions, along with those imposed under Section 404 of the Federal Clean Water Act (relating to dredge and fill permits), Section 401 (relating to state certification of water quality conditions), Section 303(d) (relating to impaired water bodies and wasteload allocations) and those which may be necessary to meet Section 319 (non-point source best management practices) as well as new watershed-based requirements may increase the costs of future operations of the Water System and development of water resources. The EPA's emphasis on watershed planning and proposed modifications to the water quality standards program involve such issues as biological criteria, antidegradation review of permitted activities and standards for clean sediment and nutrients that could further impact water project construction and operation.

The Federal Endangered Species Act requires consultation with the U.S. Fish and Wildlife Service by a federal agency before the agency issues any authorization or permit for an activity. If the U.S. Fish and Wildlife Service determines that the proposed activity will have a detrimental impact on threatened or endangered species or their habitat, it must identify a reasonable and prudent alternative which would not jeopardize the species or result in the destruction of its habitat. This process can result in decreased project yields, increased project costs or both. For example, in June 1998 the Preble's Meadow Jumping Mouse, whose habitat includes some riparian areas in and around the City, was designated as a threatened species. This designation affects construction activities in those areas by requiring special permits, development of conservation plans and consultation with the U.S. Fish and Wildlife Service. In response to this, Utilities initiated a collaborative process, which includes other regional stakeholders, to develop an appropriate local conservation plan that will allow continued construction activities without unreasonable additional regulatory requirements. In 2008, the U.S. Fish and Wildlife Service proposed critical habitat designation for the Preble's Meadow Jumping Mouse in a small portion of Utilities' service area. This proposal is not expected to have significant impact on Utilities' projects or operations.

#### ***RISK MANAGEMENT***

Utilities conducts an ongoing review of the value of its assets and its operational and enterprise risk. Utilities implemented an Enterprise Risk Management program in 2004. The program provides a governance framework to identify, quantify, prioritize and manage the significant risks of Utilities. As required under Utilities governance policies, a third party risk consultant, RW Beck, Colorado, reviewed the Enterprise Risk Management program in 2010. The review concluded the Enterprise Risk Management program meets industry standards.

The program requires specific risk mitigation policies, plans and procedures be maintained to identify significant risks, document risk mitigation plans and provide for ongoing monitoring and communication. A Risk Management Committee was established to maintain awareness of the status of prominent risk exposures and receives information on a regular basis. Utilities' Board receives semi-annual monitoring reports on Enterprise Risk Management.

Property insurance is purchased for Utilities' facilities and infrastructure (except for transmission lines, underground piping and dams) with \$500.0 million in limits and a \$1.0 million self-insured retention. Coverage for losses under the Terrorism Risk Insurance Act is purchased under the property insurance.

Excess liability coverage was purchased in 2013 with \$35.0 million in limits and a self-insured retention of \$1.0 million. A Public Officers Liability policy, including employment practices liability and Directors' and Officers', was also purchased in 2013 by the City and includes coverage for Utilities.

The Colorado Governmental Immunity Act, as recently amended, provides that the maximum amount that may be recovered through Colorado tort claims against entities such as Utilities is \$350,000 for any injury to one person in any single occurrence, and \$990,000 for any injury to two or more persons in any single

## COLORADO SPRINGS UTILITIES

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occurrence. The Colorado Governmental Immunity Act provides that the City may, by resolution, increase any maximum amount that may be recovered from the City for the type of injury described in the Act. The City Council, on July 8, 1986, adopted a resolution waiving the statutory liability limits set forth in the Colorado Governmental Immunity Act to the extent and to the limits of applicable liability policies. The City may repeal its waiver of the statutory limits at any time.

An Excess Workers' Compensation liability insurance policy was purchased for statutory benefits in excess of \$750,000 self-insured retention. Workers' compensation claims are self-insured and managed by City in-house staff. A self-insurance claim reserve fund is maintained to pay outstanding workers' compensation and liability claims. As of December 31, 2013 and 2012, Utilities' Statements of Net Position reflected the accrual for estimated probable losses for injury and damage claims of \$15,000 and \$356,407, respectively, for general liability claims. Utilities also contributes, along with the City, to a joint Workers' Compensation Self-Insurance Fund. Outstanding workers' compensation claims are reserved at \$3,154,751 under the City's self-insurance fund. The City believes that any liability arising out of unforeseen losses will not materially impact Utilities' financial position. This balance is not reflected on Utilities' Statements of Net Position.

Utilities is self-insured up to \$400,000 per individual for medical and self-insured for a limited dental benefit, and is fully insured for the vision plan. All plans provide covered employees and dependents the intended benefits detailed in the self-funded health plan documents. As part of this plan, Utilities pays claims and associated plan expenses through its Employee Benefits Self-Insurance fund. During the course of the plan year, the contributions from Utilities and employees are expected to cover projected health care expenses while maintaining a fully funded reserve account for Incurred But Not Reported ("IBNR"), Health Reimbursement Account ("HRA") and catastrophic claims. At December 31, 2013 and 2012, the plan had an ending balance of \$6,184,208 and \$7,369,166, respectively. Of the plan's ending balance, \$3,534,506 and \$3,025,656, respectively, were reserved for IBNR, the HRA and the catastrophic claims, leaving an unreserved fund balance of \$2,649,702 and \$4,343,510, respectively. Additionally, Utilities maintains a reinsurance policy through Cigna Health and Life Insurance Company, with a deductible of \$400,000 per claim per plan year. Should a covered medical claim exceed \$400,000 in a given plan year, the plan would be reimbursed by Cigna for the amount in excess of the deductible.

During 2013, there were no significant reductions in insurance coverage as compared to 2012. In the past three years, no loss occurred that required settlements in excess of coverage.

#### Summary of change in claims:

	Injuries and Damages	Employee Benefits
	(in thousands)	
Unpaid Claims - December 31, 2011	\$ 258	\$ 2,697
2012 Increases	541	17,841
2012 Decreases	(443)	(17,178)
Unpaid Claims - December 31, 2012	356	3,360
2013 Increases	445	19,674
2013 Decreases	(786)	(20,258)
Unpaid Claims - December 31, 2013	\$ 15	\$ 2,776

Note: Immaterial differences may occur due to rounding.



## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### ***LEGAL MATTERS***

In 2009, the City applied to the Colorado Water Quality Control Division (the "Division") for a 401 Certification relating to the SDS. On April 23, 2010, the Division issued its 401 Certification for the SDS. The District Attorney for the Tenth Judicial District (the "Pueblo District Attorney") and the Rocky Mountain Environmental Labor Coalition appealed the Division's 401 Certification to the Colorado Water Quality Control Commission, which upheld the 401 Certification. The Pueblo District Attorney and the Rocky Mountain Environmental Labor Coalition subsequently appealed that decision to the District Court for Pueblo County, Colorado. On April 12, 2012, the District Court ruled in favor of the District Attorney and the Rocky Mountain Environmental Labor Coalition, set aside the 401 Certification, and remanded the 401 Certification back to the Division for further consideration. The Colorado Water Quality Control Commission and the City appealed this decision to the Colorado Court of Appeals. On July 18, 2013, the Colorado Court of Appeals overruled the Pueblo County District Court and upheld the Division's original 401 Certification. The Pueblo County District Attorney has appealed such decision to the Colorado Supreme Court by filing a petition for a writ of certiorari.

Even if the Colorado Supreme Court agrees to accept the writ of certiorari and review the Court of Appeals ruling, there will be no immediate impact on the SDS. The Army Corps of Engineers issued its Section 404 permit in May, 2010, specifically incorporating the conditions and requirements of the Division's 401 Certification as issued. There is no requirement in any federal statutes or regulations that the Army Corps of Engineers must modify a previously-issued Section 404 permit if a 401 certification is invalidated or revoked. Any decision to ultimately modify the permit terms lies within the discretion of the Army Corps of Engineers, and any such decision would likely occur after a final judgment (i.e., nonappealable) has been delivered.

On September 17, 2012, the Sierra Club served Notice of Intent to Sue for Clean Air Act Violations at Utilities' Drake and Nixon Power Plants (hereafter, the "Sierra Club Notice") with respect to their coal-fired boilers. The Drake Power Plant facility fires coal as the primary fuel. It has three boilers (Units 5, 6 and 7), all of which are pulverized-coal, front-fired boilers. The Nixon Power Plant facility has one coal-fired boiler (Unit1). These are the units at issue.

The Sierra Club Notice lists 37 projects that allegedly violated the Clean Air Act. The Sierra Club Notice also alleges that the Drake and Nixon Power Plants have violated air quality permits. This matter primarily involves the New Source Review program and a subset of that program known as Prevention of Significant Deterioration. These programs require pre-construction permitting. The Sierra Club alleges that the projects at issue meet the legal criteria for a pre-construction permit. The relief sought is not specifically alleged, although the Sierra Club Notice references injunctive relief and civil penalties.

The Sierra Club Notice is not the commencement of a legal proceeding, as there has been no court filing. The outcome of this litigation, if commenced by the Sierra Club, is unclear at this time.

Utilities' Statements of Net Position as of December 31, 2013 reflected the accrual of \$15,000 for estimated liability for injury and damage claims. The City Risk Manager estimates that the amount of liability for potential claims (taking into account such accrual, the Colorado Governmental Immunity Act and insurance coverage) against Utilities would not materially affect the financial condition or operations of Utilities. Utilities has purchased insurance covering damages due to most types of major contingencies, subject to the limits in those policies and subject to the application of the Colorado Governmental Immunity Act.

On June 20, 2011, the Cascade Public Service Company and the Cascade Metropolitan District filed a complaint for declaratory relief and damages against the City and Utilities in the District Court for Water

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

Division No. 2. The complaint seeks damages for the City's alleged failure to fulfill certain contractual duties under a 1990 Water Service Agreement with the Cascade Town Company and the Cascade Public Service Company. Utilities is defending the claims, which it regards as unfounded. A trial date has been set for February 11, 2014. The outcome of this suit is unclear.

On August 2, 2013, the City was served with a complaint from Mr. Douglas Bruce, a local citizen ("Citizen") that alleges numerous causes of action, three of which involve Utilities. The Citizen alleges that the City is violating Issue 300 by receiving monies from enterprises, including the surplus payment received from Utilities and that the surplus payments represent an unauthorized tax increase under the State constitution. The City has taken the position that the payment of these surpluses is not in violation of the provisions of Issue 300. Likewise, the City does not believe the surplus payments represent unauthorized tax increases under the State constitution. The Citizen also alleges that the charges Utilities imposes to reconnect abandoned water service lines and that the imposition of watering restriction by Utilities, are in each case, a taking, and a denial of due process and equal protection. The City believes that for a variety of reasons it will prevail on all of these claims, however, the outcome of the litigation is unclear at this time.

#### **REGULATORY MATTERS**

Utilities is subject to regulation by the City Council with respect to rates charged for services, budgeting, accounting and other matters pertaining to regulated operations. As such, Utilities applies the provision of GASB 62 (formerly Statement of Financial Standards No. 71, *Accounting for the Effects of Certain Types of Regulation* [Codification 980-340-25-1]).

Effective January 1, 2012, Utilities began directly expensing conservation and demand side management rebate costs. Prior to 2012 expenses were accounted for using GASB 62. The balance of expenses accounted for using GASB 62 totaled \$7,444,057 in 2013.

Effective December 31, 2009, Utilities received approval to utilize the recognition of a regulatory asset for SDS mitigation, engineering and design expenditures specific to the monetary mitigation requirements of the Pueblo County 1041 permit, certain National Environmental Policy Act mitigations as required by the Bureau of Reclamation, and Fremont County Mitigation that do not meet Utilities' capitalization requirements and would otherwise be expensed as incurred. In 2013 and 2012, these SDS mitigation costs were \$5,341,658 and \$9,529,000, respectively.

Effective December 31, 2012, Utilities received City Council approval to recognize debt issue costs as a regulatory asset in accordance with GASB 62. A regulated asset valued at \$16,039,835 was established on January 1, 2013, for the unamortized balance of the debt issue costs through December 31, 2012. In 2013 additional debt issue costs were \$1,683,148. Debt issuance costs are amortized over the life of the bonds using the straight-line method and the expense is reported as other expense on the Statements of Revenues, Expenses and Changes in Net Position.

In addition, Utilities defers approved expenditures for the pause in construction of a capital project when it is unclear if the project will result in a future asset placed in service. If construction continues, these costs will be transferred to the appropriate utility plant account and depreciated once the project is placed in service. If the work is abandoned, the costs will be expensed in the current period.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### ***REFUNDED BONDS***

Utilities has placed proceeds from advance refunding bond issues in irrevocable refunding escrow accounts. The monies deposited in the irrevocable escrow accounts are invested in U.S. Treasury obligations that, together with interest earned thereon, would provide amounts sufficient for payment of all principal and interest on each remaining payment date, either through regular maturities or designated prior redemption dates. In accordance with the provisions of the escrow agreements, Utilities has furnished the escrow agents with certificates of independent certified public accountants as to the adequacy of the earning and principal maturities of the U.S. Treasury obligations being sufficient to pay the refunded bond issues. Accordingly, the escrow accounts and the refunded bonds are not included in Utilities' Statements of Net Position. As of December 31, 2013 and 2012, Utilities remains contingently liable for the outstanding principal balance of \$186,880,000 and \$186,235,000 in refunded bonds, respectively.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### NOTE 16 - PAYMENTS AND TRANSFERS TO THE CITY OF COLORADO SPRINGS

Utilities provides for surplus payment to the City, in lieu of taxes, based on a fixed rate per kWh (Kilo-watt hour) of electricity and Mcf (one-thousand cubic feet) at 14.65 psi of natural gas delivered within the City limits, without exclusion for interdepartmental deliveries. The payments are recorded as Transfers - surplus payments to the city on the Statements of Revenues, Expenses and Changes in Net Position. In addition, Utilities provides for other transfers when they enter into approved special contracts for water-related services that include a premium on fees and rates that benefit Utilities' ratepayers, fifty percent of the premium includes a surplus revenue and may be appropriated to the general revenues of the City by the City Council in Annual Budget and Appropriation Ordinance pursuant to the City Charter.

At December 31, the amount of Transfers on the Statements of Revenues, Expenses and Changes in Net Position and the Non-Transfer payments to the City based upon invoice dates January 1 through December 31:

	2013	2012
<b>Transfers</b>		
Surplus Payments to the City		
Electric	\$ 24,034,668	\$ 23,880,846
Natural Gas	7,809,754	6,714,420
Total Transfers - Surplus Payments to the City	31,844,422	30,595,266
 Transfers - Other		
Donala Water District Fee	187,290	210,953
Cherokee Metropolitan District Fee	120,998	428,663
Total Transfers - Other	308,288	639,616
 <b>Non-Transfer Payments</b>		
Garage and Fleet	6,156,805	6,915,596
Permits, Public Works and School Fees	3,405,049	3,734,538
Public Improvement Projects - Infrastructure	2,399,193	2,585,652
City Auditor	1,089,517	809,861
City Attorney	775,290	1,343,829
Real Estate Services	420,713	482,908
City Employee Medical Clinic and City Risk Management	393,282	122,039
Office Services	337,865	366,791
City Council	328,599	300,356
Claims and Workers Compensation	277,244	324,657
Parking	249,256	189,004
Radio	228,266	224,516
Courier Service and Postage	170,500	148,202
Pikes Peak Area Council of Governments	169,612	116,305
Senior Maintenance Tech and Landscape Architect	153,688	153,688
City Clerk	143,193	94,485
Miscellaneous Other	128,729	186,087
Police and Security	114,644	113,049
Parks Recreation - Improve Manitou Incline	-	100,000
Total Non-Transfer Payments	16,941,445	18,311,563
<b>Total Transfers and Payments to the City</b>	<b>\$ 49,094,155</b>	<b>\$ 49,546,445</b>

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### NOTE 17 - COMPONENT UNITS AND JOINT VENTURES

##### **COMPONENT UNITS - CITY**

Utilities is a participant in PACE, Fountain Valley Authority, Aurora-Colorado Springs Joint Water Authority and the Canal and Reservoir Companies. Each of these entities is treated as a component unit of the City for financial reporting purposes.

**Public Authority for Colorado Energy** - In June 2008, the City contracted to purchase approximately 20.0% of Utilities' natural gas supply needs for 30 years through a natural gas prepayment transaction with Merrill Lynch Commodities, Inc., Bank of America Corporation and Royal Bank of Canada that is financed by PACE non-recourse revenue bonds. PACE is obligated to pay the principal and interest on the PACE bonds. Utilities is obligated to purchase and pay for natural gas tendered for delivery by PACE at an index price minus a predetermined discount and is not obligated to make payments in respect to debt service on the PACE bonds.

Separate financial statements of the above component units, can be obtained from the Chief Planning and Finance Officer, Colorado Springs Utilities, P.O. Box 1103, Mail Code 950, Colorado Springs, CO 80947-0950.

**Fountain Valley Authority** - The Fountain Valley Authority constructed a water treatment plant with 18,000,000 gallons per day capacity approximately 17 miles south of the City. Utilities acts as operator of the plant under contract with the Fountain Valley Authority. Utilities is entitled to receive approximately 71.4% of the water treated at the Fountain Valley Authority plant. The remaining water is available to the other Fountain Valley Authority participants, which include the City of Fountain, the Security Water District, the Stratmoor Hills Water District and the Widefield Water and Sanitation District, each of which owns and operates a water distribution system.

Under the applicable long-term contracts relating to the Fountain Valley Authority, Utilities is obligated to pay water treatment service charges to the Fountain Valley Authority and water conveyance service charges to the U.S. Bureau of Reclamation ("Bureau") for conveyance of its water through the Bureau's Fountain Valley Conduit, which conveys raw water from the Pueblo Reservoir to the Fountain Valley Authority's treatment plant and treated water from the treatment plant to distribution reservoirs of the Fountain Valley Authority participants.

**Aurora-Colorado Springs Joint Water Authority** - The Aurora-Colorado Springs Joint Water Authority has constructed a 66-inch diameter pipeline from the Twin Lakes Dam, which is located approximately 12 miles south of Leadville, Colorado, to connect with the Otero Pumping Station intake pipeline located approximately 10 miles north of Buena Vista, Colorado. Utilities has a 66.7% participation share in the Aurora-Colorado Springs Joint Water Authority's project. This share was determined by the parties on the basis of their projected pumping demands, but no provision is made in the Aurora-Colorado Springs Joint Water Authority contracts for adjustments in participation shares if actual pumping demands differ from these projections. Therefore, it is possible that the transmission service charges to be paid by Utilities will be disproportionate to the water transmission service that Utilities is using during a particular time period.

**Canal and Reservoir Companies** - Utilities owns from 51.9% to 77.2% in four canal and reservoir companies which include The Twin Lakes Reservoir and Canal Company, The Lake Meredith Reservoir Company, The Colorado Canal Company and The Lake Henry Reservoir Company. This ownership interest represents proportionate ownership and control of the companies' facilities and water rights. The water rights add significant physical water to the water supply portfolio in addition to allowing for exchange, storage, staging and delivery of Utilities' water supply.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### **JOINT VENTURE**

**Young Gas Storage Company, Ltd. ("Young")** - Utilities has an equity interest of 5.0% in this joint venture. Young is a Colorado Limited Partnership organized on June 30, 1993, to develop and operate a natural gas storage system near Fort Morgan, Colorado. Young's natural gas storage system consists of 38 natural gas storage facility wells, a 6,000 horsepower compressor station, a natural gas processing plant, eleven miles of 20 inch transmission line and four miles of storage gathering line.

The net investment in Young reported on the Statements of Net Position as of December 31:

<u>December 31,</u>	<u>Amounts Invested</u>	<u>Undistributed Net Earnings (Losses) (in thousands)</u>	<u>Utilities Investments</u>
2013	\$ 500	\$ 698	\$ 1,198
2012	500	775	1,275

Note: Immaterial differences may occur due to rounding.

## COLORADO SPRINGS UTILITIES

### NOTES TO FINANCIAL STATEMENTS

As of and for the Years Ended December 31, 2013 and 2012

#### NOTE 18 - ADJUSTMENT OF NET POSITION FOR GASB 65

Effective for financial statements issued beginning after December 15, 2012, Utilities implemented GASB 65, *Items Previously Reported as Assets and Liabilities*, which required the effects of the implementation to be presented in the earliest period stated in the financial statements. Adjustments made to the 2012 financial statements as a result of the implementation of GASB 65:

	2012	GASB 65 Adjustment (in thousands)	2012 (Adjusted)
<b>Statements of Net Position</b>			
Noncurrent Assets:			
Unamortized debt issuance costs	\$ 16,040	\$ (16,040)	\$ -
Other (including utility acquisition adjustment)	99,196	16,040	115,236
Deferred Outflows of Resources:			
Loss on debt refundings	-	26,100	26,100
Noncurrent Liabilities:			
Revenue bonds, net of unamortized premiums and discounts	(2,237,520)	(24,356)	(2,261,876)
Deferred Inflows of Resources:			
Gain on debt refundings	-	(2,562)	(2,562)
Net Position:			
Net investment in capital assets	1,068,460	(818)	1,067,642
<b>Statements of Revenues, Expenses and Changes in Net Position</b>			
Nonoperating Revenues (Expenses):			
Other expenses	(3,788)	(1,511)	(5,299)
Interest expense	(89,565)	693	(88,872)
Total Net Position, December 31	1,454,174	(818)	1,453,356

Note: Immaterial differences may occur due to rounding.

#### NOTE 19 - EXTRAORDINARY ITEMS

In September 2013, significant rainfall and flooding occurred in Utilities' service area and surrounding areas. This rainfall and subsequent flooding were rare and unusual based upon historical rainfall patterns in the Utilities' service area. These events caused significant damage to some of the Utilities' infrastructure and assets, including some which were permanently impaired. These permanently impaired assets include the One Northfield Sedimentation Pond, the Blodgett Sedimentation Pond and the Stanley Canyon Road. The flooding in September 2013 completely covered the One Northfield Sedimentation Pond and the Blodgett Sedimentation Pond, and washed out half of the Stanley Canyon Road. These assets have a combined current value of \$507,495 and will not be repaired; an extraordinary expense in this amount has been recognized pursuant to GASB Statement No. 42 *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*.

## **COLORADO SPRINGS UTILITIES**

### **NOTES TO FINANCIAL STATEMENTS**

As of and for the Years Ended December 31, 2013 and 2012

#### **NOTE 20 - SUBSEQUENT EVENTS**

**MARKET VALUATION** - As a result of fluctuations in the SIFMA rate, LIBOR rate and other market rates since December 31, 2013, there may be a significant impact on SWAP valuation and investment valuation subsequent to the date of this report. The amount of these impacts is not known.

**RATE CHANGES** - On November 26, 2013, the City Council approved an increase to the electric and gas rates that took effect January 1, 2014.



## **REQUIRED SUPPLEMENTARY INFORMATION**

## COLORADO SPRINGS UTILITIES

REQUIRED SUPPLEMENTARY INFORMATION  
For the Years Ended December 31, 2013 and 2012  
(Unaudited)

### **OTHER POST-EMPLOYMENT BENEFITS REQUIRED SUPPLEMENTARY INFORMATION**

**Annual OPEB Cost and Net OPEB Obligation Funding Progress** - Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Between 2013 and 2011, assumptions used in the actuary study in aggregate accounted for the difference in the AAL decrease.

Schedule of funding progress:

Actuarial Valuation Date	Actuarial Value of Assets	AAL	UAAL (in thousands)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
1/1/13	\$ -	\$ 18,000	\$ 18,000	0.0%	\$ 1,555	1157.6%
1/1/11	-	18,602	18,602	0.0%	1,615	1151.8%
1/1/09	-	17,074	17,074	0.0%	1,549	1102.3%

Note: Immaterial differences may occur due to rounding.