

FAQ on SDS Contracts with the Bureau of Reclamation

Q. Why is SDS required to have contracts with the Bureau of Reclamation?

A. The Southern Delivery System (SDS) is a municipal water project for Colorado Springs Utilities, the City of Fountain, the Security Water District and the Pueblo West Metro District. The 62-mile pipeline will connect to Pueblo Dam and extend north to Colorado Springs. Because Pueblo Dam is part of the federal Fryingpan-Arkansas Project, the SDS project requires contracts with the U.S. Bureau of Reclamation for the storage, conveyance and exchange of water using those facilities.

Q. What is the Fryingpan-Arkansas Project?

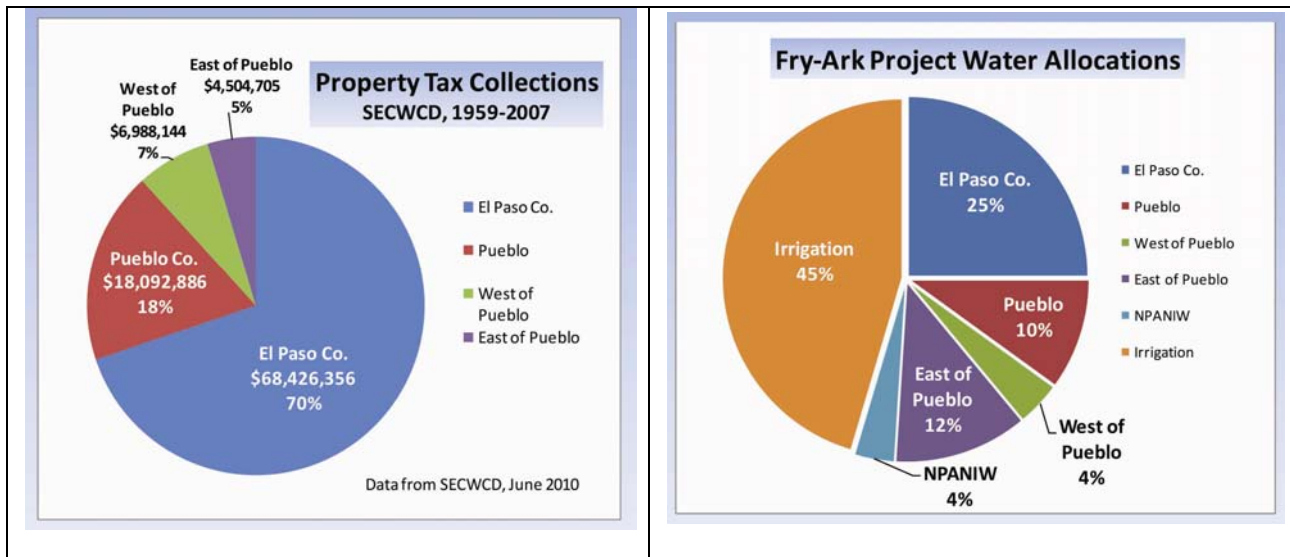
A. The Fryingpan-Arkansas Project (Fry-Ark) is a water diversion, storage and delivery project that serves southeastern Colorado. The project was authorized in 1962 for the purposes of supplying water for irrigation, municipal, domestic and industrial uses, generating and transmitting hydroelectric power and energy, and controlling floods, as well as other beneficial uses including recreation and the conservation and development of fish and wildlife. The project includes five dams and reservoirs, one federal power plant, eight tunnels, and 12 conduits. It is owned by the United States and managed by the Bureau of Reclamation. The Fry-Ark carries water from Colorado's West Slope to the East Slope. Colorado Springs, Pueblo, La Junta, Lamar, and other municipalities in southeastern Colorado, all benefit from the supplemental water the project provides.

Water is diverted from the West Slope's Fryingpan River basin and travels through a series of tunnels and small diversion dams, through a hydro power plant to Twin Lakes Reservoir near Leadville, CO. Water from Twin Lakes continues down Lake Creek to the Arkansas River, which is the main delivery vehicle for the Fry-Ark project. Pueblo Reservoir is the final reservoir in the system and delivers the majority of water for agricultural irrigation and the remainder for municipal use. Total storage space in Pueblo Reservoir is 296,885 acre feet of water.

All four SDS project partner communities are participants in the Fry-Ark Project.

Q. What has Colorado Springs paid through taxes toward Pueblo Reservoir?

A. The property owners of Colorado Springs and its partner communities' pay ad valorem taxes to the Southeastern Colorado Water Conservancy District (www.secwcd.com) that account for more than 70% of the total tax receipts – more than \$68 million through 2007 – used by the District to help repay the federal government for construction of the Fry-Ark Project facilities and to pay operation, maintenance and replacement costs.



We believe these significant contributions should be considered in setting an equitable rate charged to municipal entities that use excess capacity in the Fry-Ark Project. In fact, without El Paso County's contributions to the Fry-Ark Project through the 70% ad valorem taxes, there would be no excess storage capacity in the reservoir for Reclamation to sell because there would be no reservoir.

Q. What does Colorado Springs mean when it is asking for equity with other in-district water users?

A. The SDS partner communities, all contributors to and beneficiaries of the Fry-Ark Project, should be treated with fairness, equity, and on a level playing field with the Pueblo Board of Water Works – the only other community within the Southeastern Colorado Water Conservancy District with a long-term contract.

The Pueblo Board of Water Works has a long-term excess capacity (LTEC) storage contract with Reclamation from 2000 through 2025 at a rate of \$17.35/acre-ft for its water storage with zero annual inflation adjustment and a conveyance contract using Pueblo Reservoir with no charge other than the infrastructure investment repayment. Reclamation has proposed that SDS pay \$75/acre-ft for LTEC storage and conveyance using Pueblo Reservoir with a 3.08% annual adjustment for inflation. This table shows the inequities:

	Pueblo Board of Water Works	Southern Delivery System
Storage	\$17.35/acre-ft	\$75/acre-ft
Conveyance	\$0.00/acre-ft	
Annual Inflation Adjustment	0%	3.08%
Initial Capital Investment in Pueblo Dam Outlet Works	\$1.7 million	\$30 million paid up-front

July 12, 2010

Setting a higher price puts an unreasonable burden on our customers. Reclamation's proposal would mean more than \$200 million in additional costs for the SDS partner communities that will already face a doubling of their water rates to pay for this project.

The SDS project communities will invest an estimated \$30 million up front to construct the North Outlet Works – the infrastructure needed for conveying water from Pueblo Reservoir to the SDS pipeline. We believe it is unreasonable for Reclamation to charge the SDS communities to convey our water through the infrastructure we're constructing, funding and turning over to that agency. The new outlet in Pueblo Reservoir will benefit Reclamation and other water users by expanding the municipal/industrial capacity and providing more redundancy, as well as opportunities for future leases and revenues generated for Reclamation.

Q. What is the difference between contracts for excess capacity storage, conveyance and exchange?

A. **Excess capacity storage contracts** enable participants to store non-Fry-Ark project water in Pueblo Reservoir. SDS project participants would use existing storage capacity in the reservoir when the space is not filled up with Fry-Ark Project water or water stored through the Winter Water Storage Program.

Conveyance contracts allow a water provider to transport the water through the facilities associated with Pueblo Reservoir. In the case of SDS, the project participants are providing the up-front funding for a new \$30-million outlet or connection at Pueblo Dam – the North Outlet Works – to transport water through the dam to the SDS pipeline. The new outlet in Pueblo Reservoir will expand the municipal/industrial capacity and provide more opportunity for redundancy. It will also provide opportunity for future leases and subsequent revenues which we expect will help offset the initial up-front investment by SDS.

Exchange contracts allow for the exchange of water between Pueblo Reservoir and Reclamation's reservoirs in the Upper Arkansas River Basin, including Twin and Turquoise Reservoirs. We believe the SDS charge for exchange should be based on the actual amount of water exchanged annually, as this will occur on a limited basis.

Q. Will there be opportunities for other users, in addition to the current partners, to convey water through SDS?

A. The SDS project partners have consistently stated that if other communities within the Arkansas River Basin want to use SDS to convey their water, those communities would need to conduct their own separate environmental studies, permitting and contracting. This is spelled out clearly in the SDS Final Environmental Impact Statement and Record of Decision. The SDS partners believe the current SDS contract being negotiated should not preclude this as a future possibility and that if the required

July 12, 2010

permits, approvals and contracts are obtained, new users should be allowed to convey water through SDS.

Q. Will SDS move Fry-Ark water and non-Fry-Ark water?

A. Yes. The pipeline will be used to move both Fry-Ark Project and non-Fry-Ark Project water. SDS requires excess capacity contracts for the non-Project water moved through the Fry-Ark facilities. The excess capacity contracts are for non-Project water to be moved or exchanged through the federal project when space is available.

Q. How much is SDS seeking to store?

A. Colorado Springs is seeking a long-term contract to store up to 28,000 acre-feet of water — about what it stores now using annual short-term excess capacity contracts — in an excess-capacity account in Lake Pueblo for 2011. The other SDS partners want long-term contracts as well: Pueblo West, 10,000 acre-feet; Security, 2,500 acre-feet; Fountain, 1,500 acre-feet.

Q. What length contract are you seeking?

A. SDS project partners are asking Reclamation to approve a 38-year contract beginning Jan. 1, 2011 through Dec. 31, 2049.