



OFFICE OF THE CITY AUDITOR COLORADO SPRINGS, COLORADO

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16-07 Colorado Springs Utilities Annual External Report on Executive Limitations (4) Asset Protection and (7) Financial Conditions and Activities

April 2016

Purpose

The purpose of this review was to determine whether Colorado Springs Utilities and the Utilities Chief Executive Officer complied with the existing Executive Limitations (EL) 4, Asset Protection Policy Prohibitions 1, 4, 6, 7 & 9, and all of EL-7, the Financial Condition and Activities Policy Prohibitions for the year ended December 31, 2015. In addition to verifying management's report, the Office of the City Auditor would report any known violations if such violations were not reported by management.

Highlights

We conclude that the Chief Executive Officer was in material compliance with policy prohibitions EL-4 and EL-7. However, we noted four observations, which would enhance governance.

Our audit included the review of source documentation, detail test of calculations, and other audit procedures as we deemed necessary. We verified the accuracy and reliability of the statements made along with information presented in the EL-4 and EL-7 reports prepared by Colorado Springs Utilities for the Utilities Board. We also relied on the major transaction systems audit work performed by our office, as well as, the work of the external auditors.

The Utilities Board monitored the organization's operations through boundaries established by the Executive Limitations Policies. The Office of the City Auditor annually verifies compliance with Executive Limitations 4 and 7. Key components of the prohibitions were:

- Asset Protection (EL-4) - required that Colorado Springs Utilities have policies and procedures in place that ensure sound business practices to protect assets. These included purchasing and real estate regulations, investment procedures, bonding requirements for personnel with access to funds, and controls over receipt and disbursement of funds.
- Financial Condition and Activities (EL 7)- required compliance with financial measures such as cash on hand and debt service coverage. Additionally, this limitation required management to inform the Utilities Board of expenditures in excess of appropriations and major new or cancelled projects.

Recommendations

- 1) The City's Real Estate Services office and Utilities should improve processes related to reporting and filing to improve accuracy and completeness of required EL 4 reporting.
- 2) The Utilities Board should consider whether the EL 7, limitation 2 should include a report of all projects that exceed \$500,000 not funded in the budget and actual to budget results for all major capital projects.
- 3) Utilities should improve accuracy of depreciation forecasts and related EL 7 reporting.
- 4) The Utilities Board should determine whether the annual EL 7 report should include segment reporting as supplemental information. The EL reporting date may need to be adjusted accordingly.

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Observation 1

In support of EL 4, limitation 9 regarding written land acquisition regulations, the City's Real Estate Services office provides support to Colorado Springs Utilities for all land transactions.

(1) Errors were found in both semi-annual EL 4 reports prepared in 2015. Two transactions were reported at the wrong amount by City Real Estate Services and one was missing from the report by Utilities. The total amount was also incorrectly reported. (2) Additionally, of the twenty files reviewed, six did not contain all required paperwork. The missing documents were obtained once the omission was discovered.

City Management Response:

City response: Colorado Springs Real Estate Services agrees with the observation and will review our processes for recordation tracking and filing of required documents. We will work with Colorado Springs Utilities to identify opportunities to improve the EL-4 reporting process.

Utilities Management Response:

Utilities' staff will work closely with City staff to insure the reporting in EL4 is accurate.

Recommendation

- 1) The City's Real Estate Services office and Colorado Springs Utilities should work together to improve processes for reporting real estate transactions.
- 2) The City's Real Estate Services office should improve recordation processes and improve filing of required documents for acquisitions.

Observation 2

Under EL 7 limitation 2, Utilities reported new projects over \$500,000 not funded in the approved budget or cancelled projects over this amount. Utilities complied with this limitation.

However, actual spending by major project, and significant budget changes to existing projects were not reported. If a project was added for under \$500,000 but more than \$500,000 was spent, this was not required to be reported. Similarly, when projects exceed budget by a significant amount, this was not required to be reported.

Reports of actual spending against budget by major project would inform governance of performance against the approved capital plan.

Management Response:

Colorado Springs Utilities feels that it has met the obligations in EL7, Limitation 2. Analysis of actual spending by project is reported in the Financial Reporting Package which is provided to Finance Committee and the Board on a monthly basis.

Recommendation

The Utilities Board should consider whether the EL 7, limitation 2 should include a report of all projects that exceed \$500,000 not funded in the budget and actual to budget results for all major capital projects.

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Observation 3

The 4th quarter 2015 EL 7 limitation 1 reported that Operations and Maintenance expense was under budget by 15% for 2015. The EL report did not indicate that 5% or \$28 million of the 15% variance was related to depreciation, a non-cash expense. If depreciation expense was not included, the Operations and Maintenance budget variance was 10% for 2015.

The Annual Operation Plan's budgeted depreciation expense has been on average 18% higher than actuals the last four years. While the variance is significant it is a low risk item because depreciation did not affect rate-setting and was not included in the appropriation as it was a non-cash expense.

Management Response:

Colorado Springs Utilities is working on improving the accuracy of depreciation. Large dollar amounts in Construction Work In Progress for SDS and Emission Controls have created the majority of the variance. Moving forward depreciation will be called out separately in the EL.

Recommendation

- Utilities should improve accuracy of depreciation forecasts.
- Reports of actual spending against the appropriation should exclude depreciation expense, which was not part of the appropriation.
- The explanation of budget variances related to depreciation should be accurate.

Observation 4

The final 2015 EL 7 report dated March 9, 2016 did not include financial results by service for Electric, Gas, Water and Wastewater as supplemental information. Statements by service segment were not available until April, after the date the EL 7 report was submitted to governance. The segment information was not available for the Office of City Auditor review of ELs.

Supplemental by-service results provide valuable information on the relative performance and financial status of each business segment.

Management Response:

Due to the nature of the year end accounting close and audit, by-service financials are not available until after the EL7 due date.

Recommendation

The Utilities Board should determine whether the annual EL 7 report should include segment reporting as supplemental information.

If segment reporting is desired, the EL reporting date may need to be adjusted accordingly.