

PETROS & WHITE LLC  
ATTORNEYS AT LAW

MEMORANDUM

ATTORNEY-CLIENT COMMUNICATION  
PRIVILEGED AND CONFIDENTIAL

TO: KIM HEADLEY, GARY RASO AND DAN KOGOVSEK  
FROM: RAYMOND L. PETROS, JR.  
DATE: AUGUST 7, 2009 *RLP*  
RE: EFFECT OF SDS POSTPONEMENT ON 1041 PERMIT DEADLINES

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According to recent news reports, the Colorado Springs City Counsel, has voted to postpone the construction of most components of the SDS Project for at least four years later than original projections. Colorado Springs proposes to begin construction at the Pueblo Dam and the pipeline through Pueblo West sometime in 2010 (one year later than set forth in the SDS Permit). However, it is now projected the pipeline will not be operational until 2016, rather than 2012. Also, the Terminal Reservoir in Upper Williams Creek and the Exchange Reservoir in Lower Williams Creek are now expected to be completed in years 2020 to 2025, several years later than the 2015 – 2017 timeframe set forth in the SDS Permit for the Terminal Reservoir, and 2021 – 2024 for the Exchange Reservoir.

This voluntary postponement of the SDS Project affects deadlines set forth in the SDS Permit, as follows:

1. Three-Year Lapse of Permit. Condition #1 of the SDS Permit requires that the Applicant take substantial steps to construct the “permitted development” by April 21, 2012 or the Permit may be revoked or suspended by the County. The Applicant, may, however, submit a written request for an extension of time for good cause. In order to comply with this condition, it appears that Colorado Springs’ strategy is to commence pipeline construction and the modification of the North Outlet works within this three-year period. The question then becomes whether this work will constitute “substantial steps to construct the permitted development within thirty six months from the date of the Permit.” Colorado Springs now forecasts the “permitted development” (i.e. an operational pipeline) will not occur by April 21, 2012, but instead 2016.

2. Material Change in Construction of the Project. Condition #5 states that “any material change in either the construction, use or operation (exceeding 78 m.g.d. pumping by the Juniper Pump Station) of the SDS Project from that approved”, or “with the Applicant’s performance of the terms and conditions approved in the Permit”, shall require a permit amendment. “For these purposes, a material change shall be any change in the Project which significantly changes the nature of impacts addressed by the Project.” Given the anticipated

construction schedule set forth in the 1041 Permit, the question becomes whether the postponement of the SDS Project constitutes a "material change." The postponement will, for example, delay the \$50 million monetary mitigation payments for Fountain Creek improvements. The postponement will also delay the expected flow management on Fountain Creek anticipated with the construction of the Exchange Reservoir on Fountain Creek.

3. \$300,000.00 Monetary Mitigation Payments. The three annual payments of \$100,000.00 commencing July 1, 2009 for flood control studies will not be effected by the postponement. The payment schedule is fixed pursuant to Condition #6, to begin July 1, 2009 and on each of the two anniversary dates thereafter. I understand from Dan Kogovsek that Utilities has agreed to pay the District the initial \$100,000 due last month.

4. \$50 Million Monetary Mitigation Payment. Under Condition #6, the five annual payments of \$10 million commence on January 15 of the year following completion and commencement of water deliveries through the SDS pipeline from Pueblo Reservoir to Colorado Springs. In the event completion of the SDS Project is delayed beyond October 21, 2012 because of an affirmative decision made by the Applicant, then the payments to be made by the Applicant shall begin to be made on such date, without regard to project construction status, or such payment shall be subject to annual indexing using the Colorado Front Range Producer Price Index, but not to exceed a maximum annual increase of 3.5%. Consequently, the postponement will trigger the election by Colorado Springs to either make the payment commencing on January 15, 2013 or incur interest at the modest rate of 3.5%. Under the revised construction schedule, the annual installments of \$10 million would not begin until January 15, 2017, provided Utilities is willing to pay interest. Such a delay in payment could be a setback for the organization of the Fountain Creek Flood Control District. Because this payment delay was specifically provided for in the Permit terms and conditions, arguably a delay in payments alone would not constitute a "material change" for purposes of requiring an amendment to the Permit.

5. Dredging in Fountain Creek in Pueblo. Under Condition #8, Colorado Springs committed to dredging and to construction of sediment collection devices in Fountain Creek through Pueblo. "These efforts will occur prior to construction of the SDS Project." The postponement may at most delay the dredging and construction of sediment collection devices in Fountain Creek by about one year.

6. \$75 Million Waste Water System Improvements. Condition #7 requires Colorado Springs Utilities to invest an additional \$75 million in waste water system improvements between January 1, 2009 and December 31, 2024. The postponement will not extend the due dates for these improvements, but as a practical matter, Colorado Springs may delay expenditures as long as possible toward the 2024 deadline. Under this Condition #7, Utilities also must provide Pueblo County an annual report describing such expenditures, beginning in January 31, 2010; the postponement will not effect this reporting deadline.

I am attaching copies of the Chieftain and Gazette news reports of the postponement and also the Springs' staff report recommending the postponement. I will send you a copy of the Utilities board' minutes reflecting its decision to postpone SDS as soon as they are published on the Springs' website. We should place and preserve these documents in the County SDS Permit file. These documents will prove that the delay in SDS is attributable to an "affirmative decision" by the Applicant for purposes of requiring interest on the \$50 million payments.

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Attachments