MEMORANDUM
SEPTEMBER 4, 2018

TO: BOARD OF DIRECTORS

FROM: ANDY MUELLER, GENERAL MANAGER
IAN PHILIPS, CHIEF ACCOUNTANT
PETER FLEMING, GENERAL COUNSEL
JOHN CURRIER, CHIEF ENGINEER
CHRIS TREESE, EXTERNAL AFFAIRS MANAGER
AUDREY TURNER, ADMINISTRATIVE CHIEF

SUBJECT: ***2019 BUDGET***

Strategic Plan Initiative:

12. Financial Sustainability: *The above strategic initiatives cannot be achieved without financial sustainability. The River District enjoys a diversified tax base for its Governmental Funds, which helps to reduce the impacts of dramatic downturns in its overall assessed valuation. Over the long-term, the Enterprise Fund is intended to be self-sustaining, managing the River District's Business-Type Activities.*

Strategic Initiatives
12. A. *The River District will evaluate all projects and investments for the potential impact on cash flows.*

INTRODUCTION

The annual budget workshop provides the Board and staff with an opportunity to discuss policy issues related to the District financial matters. For 2019, as always, we face a number of interesting, but manageable challenges.

The River District has three budgets; the General Fund, the Capital Projects Fund and the Enterprise Fund. The General Fund revenues are derived from property taxes and specific ownership taxes. Expenditures are primarily for staff salaries, overhead and expenses, board expenses, administrative expenses, legal and special counsel, external affairs, and technical support.

The Capital Projects Fund revenues include a small amount of earned interest and historically also included appropriations and unspent balances from the General Fund. The Capital Projects Fund is used to pay for District owned capital assets such as improvements to the building, computers, and fleet vehicle purchases and in the recent past, it has funded our grant program.

The Enterprise Fund covers the operation of active projects. Revenues are from water sales, the Denver lease (transitioning to smaller O&M payments in 2020), occasional grants and cooperative projects. No District tax revenues are deposited or booked into the Enterprise Fund.

HIGHLIGHTS BY FUND

General Fund Revenue Trend

Since 2011 our net property tax and specific ownership tax revenues have essentially been flat and certainly below the rate of inflation. Attached are graphs showing the assessed valuation and levy from 2002 and General Fund revenues from 2011-2018. In 2012 our net property tax receipts were $4.232 million. In 2019, we anticipate receiving $4.337 million. The 2018 county valuations came in at 1.05% above 2017 figures, which translates into a slight increase in budgeted tax revenue of $107,661, using the maximum mill levy allowed per Board Policy of .252 mills. This increase is well below our TABOR limitation (inflation plus new growth) of 4.38%.

2019 is a reassessment year for property tax and there is a reasonable increase in residential construction activity in the District and oil and gas exploration and production appears to be on a mild upswing as a result of increased market prices for those commodities. As such, we would normally anticipate an increase in revenue in 2020, however, due to the potential effects of the Gallagher Amendment, we are actually anticipating a potential drop in revenue of approximately 8% or $370,000.00. The management team has spent considerable time examining the potential long term impacts of the Gallagher Amendment on our District's revenues and its impact on our ability to continue to meet our mission during these critical times. Please See Chris Treese's memo on Gallagher included in your binders. I look forward to a full discussion of this issue at the Budget workshop.

General Fund Expense Trend

As has been previously discussed, the District has faced increasing expenses while maintaining relatively flat revenue. This is not a sustainable financial model. In the fall of 2017 the District adopted a 2018 Budget which showed anticipated deficit spending of over 500k. We have reduced that deficit spending to just over 230k in the proposed amended 2018 budget enclosed in this packet. It is District management's goal not to request a budget showing a net loss for our operations. As such, we have reduced our proposed expenses in 2019. In 2020, our proposed budget anticipates the full potential $370,000 reduction in revenue resulting from Gallagher (you have to plan for the worst case scenario) and as such contains extensive cuts to many of our programs and reflects an anticipated reduction in the number of District employees. Our 2019 reduction in salaries and benefits reflect the fact that we have not and do not intend to replace the Deputy General Manager and we will not have overlapping General Managers as we did in 2018. Our 2020 Budget reflects a further reduction in workforce at the District. As many of you will remember, the District increased its staff size recently in anticipation of retirements by some of our longstanding staff members. In 2019 it is likely that we will see and perhaps incentivize some of those retirements in order to help bring our salary expenses under control. It is important to point out that we do not anticipate any significant transfer of funds from the General Fund to the Capital Fund in 2018, 2019 or 2020.

CRCA Implementation

The General Fund bears the burden of our CRCA implementation costs. Beginning in late 2014, through July 2018, this effort has expended over $812,000. It is anticipated that the 2018 CRCA implementation expense will be around $150,000. In 2019 we anticipate CRCA Implementation expense to remain close to the 2018 expenses. Please keep in mind that the District is now responsible for 100% of the expenses related to these (budgeted) CRCA Implementation efforts as we have collected all pledged contributions in 2017. Those collected funds are reflected as part of the carryover balance in the General Fund but will not be considered offsetting revenue as we make our CRCA expenditures over the next couple of years.

Capital Fund

In 2013, the District spent almost $6 million on purchasing Ruedi Reservoir water. This transaction depleted the balance in the Capital Fund to about $2.5 million. The fund slowly recovered between 2013 and 2018. Our end of 2018 balance is budgeted to be $3.9 million. Due, however, to growth in General Fund expenses, we do not anticipate any transfer to the Capital Fund from the 2018 General Fund operation. For the 2018 budget, we have included $265,000 of expenditures out of the Capital Fund which includes expenditures of $150,000 for our grant program. The Board has indicated that the grant program is important and worth continuing to fund. However, in light of our current operating costs and our Gallagher impacted revenues in 2020 and beyond, your management team encourages the Board to seriously consider terminating or at least suspending the grant program. As I mentioned above, we do not project an ability to make significant transfers into the Capital fund in 2018, 2019 or 2020 despite significant cuts to expenses reflected in that proposed budget. Simply put, spending our District's capital reserves on grants to third parties may not be a wise financial move at this point in time.

Enterprise

In 2018 we started the year with approximately $23.2 million in our Enterprise fund. In 2019, we anticipate starting the year with $25.2 million and by 2020 we anticipate a starting balance of $27.1 million. While this is a positive trend, it is largely due to our three million dollar annual lease payment we have been receiving from Denver Water over the last 20 years. In 2020 we will receive the last installment of $1.5 million. At that point anticipate receiving approximately $500k in annual O & M payments from Denver, but the hit to our ongoing income in the Enterprise fund will be significant. In 2019, our water sales may receive a 220k bump due to our recent agreement with the CWCB to lease water for winter de-icing in the Fryingpan River and we anticipate some minor additional revenue from leases to the recovery program in late 2018 due to the dry conditions on the Yampa this year. The District will need to develop additional approaches to monetizing our water assets to increase the revenue to the Enterprise as we move forward.

Our expenses in the Enterprise are higher in 2018 due to the ongoing crest restoration at Wolford Mountain Reservoir which swung into full gear today and is hopefully on track for an early October conclusion. Those dam deformation expenses are expected to be less in the foreseeable future, however, we do anticipate incurring significant expense over the next few years in an effort to repair and restore several valves and gates at the outlet works.

Pursuant to Board policy many of our operational expenses are split 75% to the General Fund and 25% to the Enterprise Fund based upon an estimate of the relative amount of time and resources spent between the two types of activities. The 2019 and 2020 Enterprise budgets reflect a reduction in those expenses which it shares with the General Fund which is largely driven by the anticipated Gallagher reduction to the General Fund, however, these reductions of expenditures in the Enterprise are welcome as a small step toward becoming more self-sustaining.

GENERAL ADMINSTRATION

Salaries and Benefits

The 2019 budget includes a salary increase pool amounting to a 3.2% increase to existing salaries which is consistent with the results of the Employers Council's (EC) "resort" survey information published in March 2018. In 2018, we budgeted an average increase to salaries that was consistent with the EC survey results, although we had used a number lower than the survey results in 2016 and 2017 to slow down wage growth. We anticipate the salary ranges will be increased by 2.2% in 2019. Additionally, we are in the process of conducting the triennial salary survey, utilizing the consulting services of Employers Council. We expect to present the findings from the survey at the October quarterly meeting. Individual position salary ranges may need to be adjusted in addition to the 2.2% based on the results of the survey.

The 2018 salaries budget reflects an overlap in the General Manager position for approximately 8 months with Eric's transition and several months of Deputy General Manager vacation pay therefore, even with the 3.2% increase in salaries, we still are budgeting for a reduction in the total salaries budget in 2019. We are showing a further decrease in salaries and overhead in 2020 which is in anticipation of reduced revenues due to the Gallagher Amendment.

The Western Slope Health Care Group is in a good position in 2018 with moderate claims, although at the time of this memo, I am budgeting for a 9% increase in premiums. The broker is currently in negotiations with the reinsurer so I anticipate that number to decrease. I will provide an update at the workshop. However, even with a 9% increase in premiums, our 5-year average health insurance expense per employee is 3.1%. Because we are below the 5% average as allowed for in the Board policy, we recommend that we continue a contribution to employee's health savings accounts in 2019 at the same level as 2018 and will also continue to require employees to contribute $150/month for dependents over age 19. Under the proposed budget, Employees will also not experience any changes to their benefits or deductibles in 2019.

Dental insurance premiums are increasing by 5.5% with no plan or provider changes. Long term disability premiums will remain the same while short term disability premiums will increase by 9%, the first increase in premiums in years.

In 2019, we recommend maintaining the 457/RHS matching at $2,400 per employee. As a cost-saving measure, the District discontinued paying out any excess medical leave above the accrual limit of 720 hours in 2017.

Capital Expenditures

We have reduced the number of fleet vehicles in 2018 by two and have budgeted to replace one of the higher mileage vehicles in 2019.

There have not been any significant building improvements or expenditures in 2018, though there is a contingency amount budgeted in 2019 for potential improvements to our office and the first floor restrooms of which we would only be responsible for our pro-rata share of the total expense as it is a common element of the condominium association. There is also a small budget for office furniture as old workstations need to be replaced.

We have budgeted for one server upgrade in 2018 and one in 2019 as well as other routine computer replacements.

LEGAL

The proposed 2018 final budget and the proposed 2019 budget for legal/special counsel are included in the summary sheets for the General and Enterprise budgets. The primary legal costs this year have been attributable to special counsel costs related to CRCA Implementation matters. In addition, CRCA Implementation items for expert consultants and other related work have been inserted into legal line-item budgets in order to facilitate accounting for various work projects related to CRCA Implementation. We propose a final 2018 legal budget be adopted in the amount of $363,000 (General and Enterprise total). The originally approved 2018 budget for legal/special counsel was $508,000.

We previously have discussed that the River District has historically allocated unspent General Account funds (including unspent General Legal Account funds) into the River District's Capital Fund. In past years, the amount of unspent legal funds provided a substantial component of the allocation to the Capital Fund. This year, we anticipate that there may be unspent legal budget funds allocated to the Capital Fund again but, as in 2016 and 2017, the amount will be less than it was historically. This reduced contribution is due primarily to reductions in the initially-approved legal budget over the years, and less attributable to any increases in actual legal and special counsel costs.

The proposed budget for 2019 for the General and Enterprise Funds totals $350,719 – a substantial reduction from the initially-approved 2018 budget. The proposed 2019 budget contemplates continuing special counsel and expert consultant expenses attributable toward CRCA

Implementation matters, some other work related to Federal Energy Regulatory Commission proceedings, and to address occasional work load issues.

EXTERNAL AFFAIRS

The 2019 EA budget includes budgeted funds for the District's triennial survey of constituents.

The EA departmental expense reductions to meet balanced budget goals are focused in educational programs and travel. External Affairs will continue to do more with less, we'll just have to be smarter, more strategic and cost-conscious.

As has been our practice, the EA budget for the out-year (2020) reflects the possible retirement of Dan Williams and the need to replace the very favorable lobbying contract we enjoy with Dan at the Denver Capitol. The 2020 budget reflects an increase – but smaller than previously forecast – but still a placeholder for a new lobbyist contract.

TECHNICAL

General Fund

For 2019 the Technical Support line items in the General Fund budget total $492,409, down from $656,000 budgeted for 2018. ***Approximately $100,000 of the difference is not truly a cost savings*** but reflects how $100,000 in revenue from our USGS program funding partners is accounted. Previously the total cost of the USGS program has been included in the budget. For 2019 the net cost of the program is included. The other (approximately) $60,000 in budget reduction reflects reduced amounts in several line items which may limit the River District's flexibility to respond to requests for assistance received in 2019.

The proposed amended 2018 budget is $606,509 compared to $656,121 originally budgeted, a decrease of approximately $50,000. This reduction is predominantly accounted for by two factors: 1) the USGS line items have been decreased by approximately $100,000 to reflect net cost to the River District, and 2) the Division 5 Work Plan line item has been increased by $50,000 to reflect funding of the GVWUA Conserved Consumptive Use Pilot Project authorized by the Board in 2018.

As always, the largest portion of General Fund Technical Support budget is for the USGS stream gauging program. The total amount budgeted for the program for 2019 is $299,409 ($395,262 with funding partner revenue included). This is identical to the 2018 budget. By keeping the budget flat it is very likely that the USGS program will need to be strategically reduced. The River District is the USGS's largest single cooperating agency in Colorado and critically important to maintaining the streamflow and water quality data relied upon by our constituents and the entire state. Any possible reductions in this program must be carefully managed to maintain the critical data relied upon by our constituents.

Other (but not all) major line items under Technical Support include; 1) salinity/selenium coordination, primarily for the Grand Valley, 2) project development work on River District conditional water rights and, 3) support for local and basin-wide cloud seeding programs and, 4) ESA/Recovery Program support.

Enterprise Fund

The Enterprise Fund technical budget covers, among many things; 1) Wolford, 2) Elkhead, 3) Eagle Park Reservoir Company, 4) capital and O&M costs for River District Ruedi Reservoir contracts, 5) cooperative management which is a "catch all" for items such as the water bank and, 6) RCPP related efforts. The Enterprise Fund includes all line items that benefit from TABOR impacted grant funding. As such the budget reflects many items that are either partially or totally offset by grant or pass-through monies.

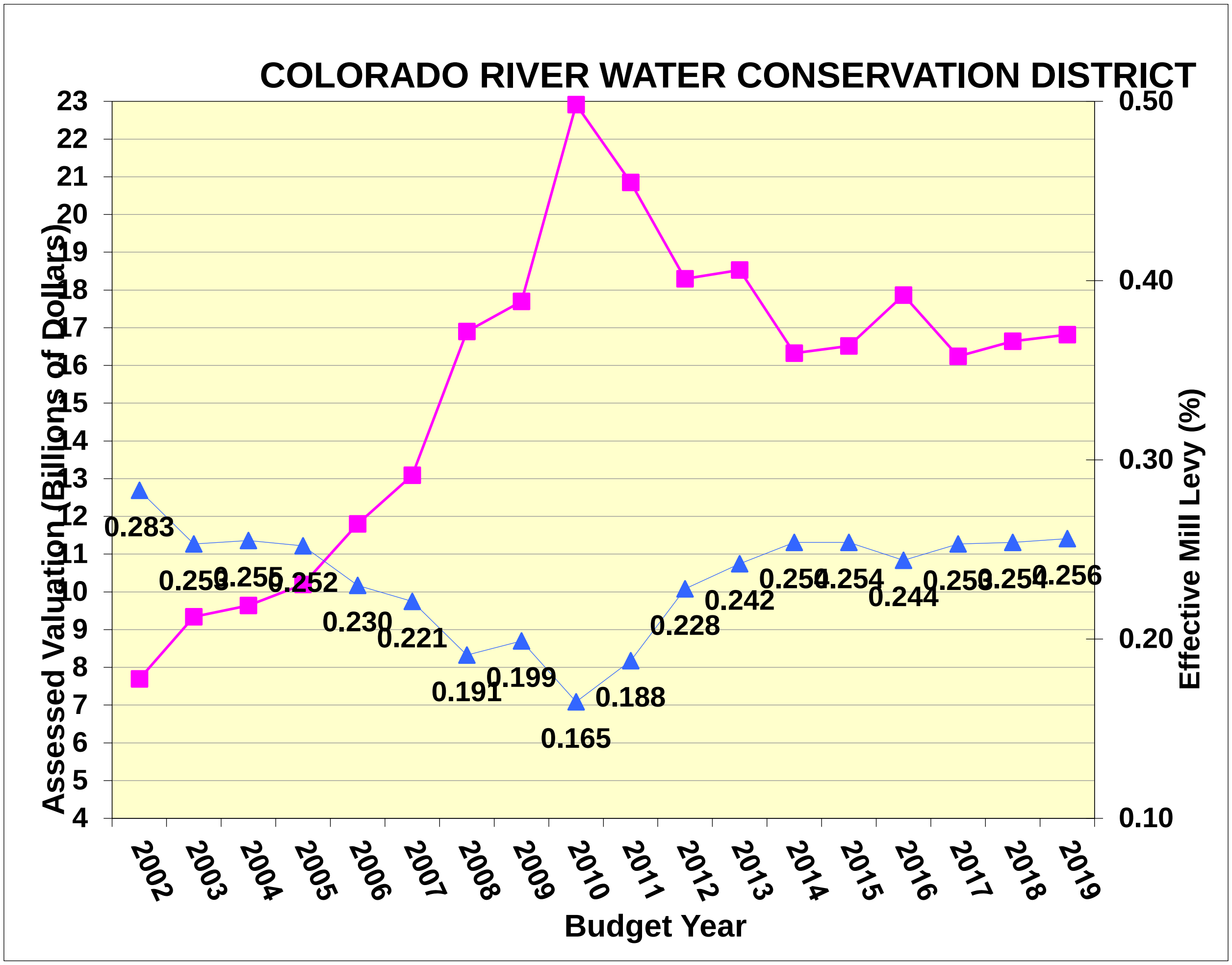
Several specific Enterprise Fund items are highlighted below.

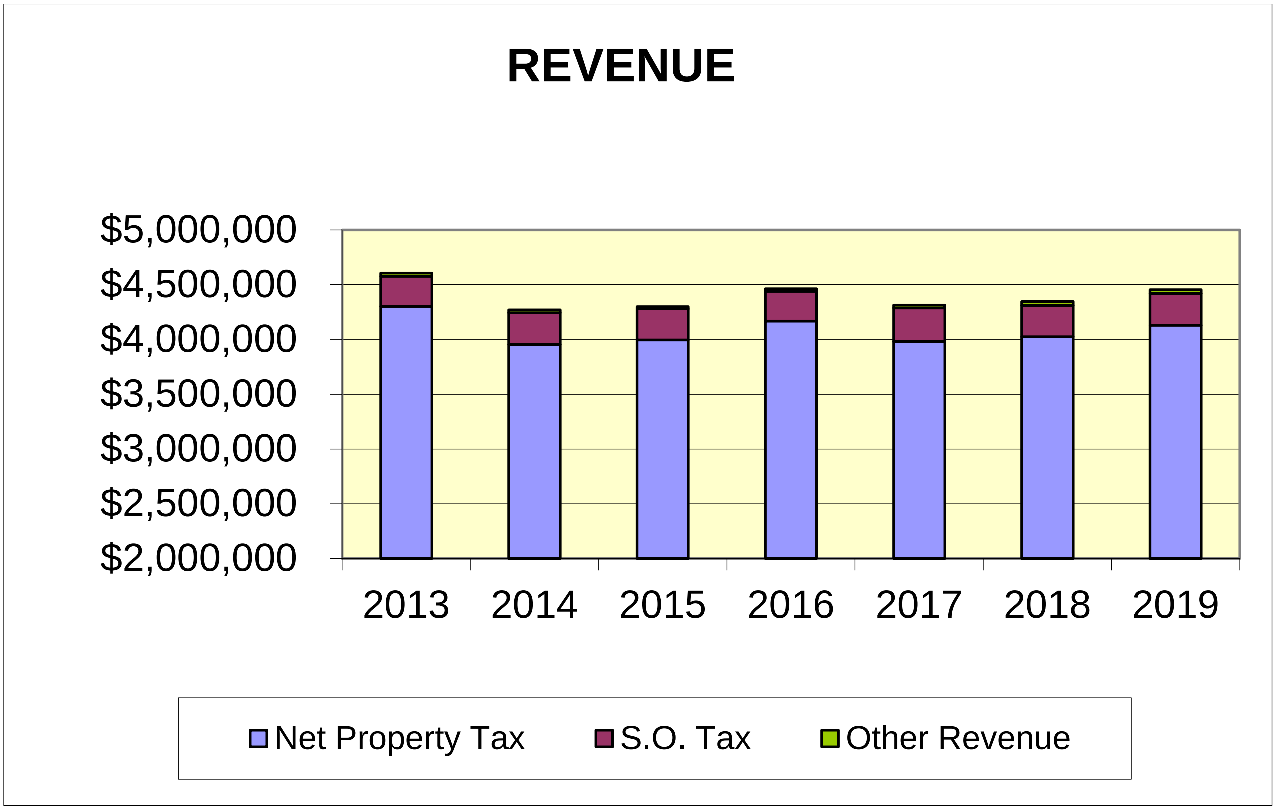
Wolford Dam Deformation. Since the decision in 2016 that there is no foreseeable need to remediate the dam, the primary focus has been on continued monitoring and restoring the crest height (topdressing). The 2018 budget was set at $500,000 which included $400,000 for topdressing the dam and $100,000 for an emergency contracting fund. Actual cost for the topdressing and continued monitoring is expected to be $635,000 in 2018 and is reflected in the proposed amended 2018 budget. Minimal work is expected in 2019 and the budget is set at $100,000.

Wolford Mitigation Area Maintenance. 2018 stream stabilization work on Muddy Creek below the dam was budgeted at $200,000. Staff has determined that it is appropriate to move slowly on the recommended improvements, therefore little activity has occurred in 2018 and the proposed amended 2018 budget has been reduced to $35,000. The proposed 2019 budget is set at $40,000, again reflecting the decision to move slowly on recommended improvements.

Wolford Reservoir Operations. This includes all costs associated with "normal" operation maintenance and repair (OM&R) of the dam, reservoir and recreation area. The amount budgeted for 2019 is $597,450. The major work task is replacement of the 96" low level outlet works gate, scheduled for completion before the start of fill in 2019. The budget amount includes a $200,000 contingency.

Elkhead – (Yampa River Projects). 2019 is expected to be a quiet year at Elkhead as reflected in the proposed budget of $177,507, down from a proposed amended 2018 budget of $214,851. In 2016 the spillway net was installed (entirely reimbursed with $500,000 from the CWCB's species conservation trust fund and $800,000 from the Recovery Program). In 2017 the failing outlet gate stem guide anchor bolts were replaced and the outlet works discharge valve was entirely refurbished. 2018 work includes redoing the stem guide anchor bolts (at the contractor's expense), conducting spillway concrete repairs and reconstructing the Malburg Pond embankment. With these projects in the rear view mirror we are planning for a very quiet year in 2019 and beyond.


COLORADO RIVER WATER CONSERVATION DISTRICT
Assessed Valuation (Billions of Dollars)
Effective Mill Levy (%)
Budget Year
0.283
0.253
0.255
0.252
0.230
0.221
0.191
0.199
0.165
0.188
0.228
0.242
0.254
0.254
0.244
0.253
0.254
0.256


REVENUE
$5,000,000
$4,500,000
$4,000,000
$3,500,000
$3,000,000
$2,500,000
$2,000,000
2013
2014
2015
2016
2017
2018
2019
Net Property Tax
S.O. Tax
Other Revenue