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May 13, 2016

HintonBurdick, PLLC
63 South 300 East, Suite 100
St. George, UT 84770

Via email

RE: City of Salida (the "City")

Dear HintonBurdick:

By letter dated May 6, 2016, Jan Schmidt, *i.e.*, the Director of Finance and Administrative Services for the City, requested that we furnish you with certain information in connection with your examination of the accounts of the City. This response is effective as of May 6, 2016.

In particular, Ms. Schmidt requested that we provide you with information relating to all material "pending or threatened litigation, claims, and assessment (excluding unasserted claims and assessments)" that our firm is handling on the City's behalf and "that existed as of December 31, 2015, and during the period from that date to the effective date of [this] response."

We did not begin work on behalf of the City until we were effectively retained and received direction from the City Council to act in that capacity on March 2, 2016. Accordingly, we offer no opinion on material pending or threatened litigation, claims or assessments that may or may not have existed as of December 31, 2015 and through March 1, 2016 and would refer any related inquiries to the former City Attorney and/or special counsel to the City.

Ms. Schmidt requested that we provide you with a description of all pending or threatened litigation, claims or assessments that we are handling on the City's behalf and that our description of each matter include the following:

- (1) the nature of the litigation [claim or assessment];
- (2) the progress of the matter to date;
- (3) how management of the City is responding or intends to respond to the litigation [claim or assessment]; and
- (4) an evaluation of the likelihood of an unfavorable outcome and an estimate, if one exists, of the amount or range of potential loss.

Ms. Schmidt also asked that we identify any pending or threatened litigation, claims, and assessments that we have been engaged on but have not devoted substantive attention. And Ms. Schmidt asked us to confirm that there are no unasserted possible claims or assessments that are probable of assertion, and that our firm will advise and consult with the City regarding the disclosure of and accounting standards relevant to any such unasserted possible claims or assessments.

Our response is based on the actual knowledge of the individual attorneys at this firm, and solely in their capacity as counsel providing legal services to the City since March 2, 2016. Our response also is limited by and in accordance with the ABA Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information and related Commentary (the "ABA Policy Statement"). Without limiting the generality of the foregoing, the limitations set forth in the ABA Policy Statement on the scope and use of this response are specifically incorporated herein by reference and any description of "loss contingencies" herein is qualified in its entirety by the ABA Policy Statement.

Our engagement by the City has been limited to specific matters, and there may exist matters of a legal nature which could have a bearing on the City's financial condition with respect to which we have not been consulted.

By making the request set forth in Ms. Schmidt's letter, the City does not waive the attorney-client privilege with respect to any information that the City has furnished to us. In addition, our response to you should not be construed in any way to constitute a waiver of the attorney work-product privilege with respect to any of our files involving the City.

I. Pending Litigation, Claims and Assessments.

This firm has represented or represents the City in connection with eight litigation matters in state court, and has not been engaged for any other litigation purposes. The firm has no knowledge of any other litigation, claims or assessments involving matters on which we have been engaged by the City as its counsel and to which we have devoted substantive attention in the form of legal representation or consultation.

A. *Steve Tafoya v. City of Salida and the City Council thereof; Diesslin Structures, Inc.*, Chaffee County District Court, Case No. 2015CV30043.

The Plaintiff in this case filed a Complaint on or about September 29, 2015, alleging that the City erred in awarding a construction contract change order by Resolution to Diesslin Structures, Inc. without engaging in an open bid process. The City defended this matter through insurance defense counsel approved by the Colorado Intergovernmental Risk Sharing Agency ("CIRSA").

On February 16, 2016, the City Council adopted Resolution No 2016 – 17 and approved a proposed Settlement Agreement and Stipulation for Dismissal with Prejudice with respect to this matter. The Stipulation provides that “the Defendant City of Salida has agreed to pay Plaintiff \$190 in attorney fees and up to \$345.00 in costs” pursuant to the Settlement Agreement. The Settlement Agreement in turn provides that “[t]he City shall pay Plaintiff \$190.00 for attorney’s fees and up to \$325.00 in reasonable costs” upon provision of incurred cost documentation.

It is our understanding that the City has not satisfied its obligations under the Stipulation and Settlement Agreement yet. We have not analyzed whether the City and/or CIRSA will be responsible for any outstanding obligations to the Plaintiff in this matter. In any case, any potential loss should be limited to Plaintiff’s maximum cost and fee recovery entitlement of between \$515.00 and \$535.00 and any related costs or fees incurred by the City.

B. *Jeff Auxier v. Jan Schmidt, et al*, Chaffee County District Court, Case No. 2013CV30068;

Jeff Auxier v. Jan Schmidt, et al, Colorado Court of Appeals, Case No. 14CA1092;

Jeff Auxier v. Jan Schmidt, et al, Colorado Supreme Court, Case No. 15SC939.

The Plaintiff in these companion cases filed a series of actions alleging that the City engaged in improper budgeting practices. The City ultimately prevailed at the Colorado Supreme Court on or about February 29, 2016 and reserved a claim for recoverable costs and/or fees in the amount of \$1,896.00. The City defended this matter through insurance defense counsel approved by CIRSA.

On April 19, 2016, the City Council adopted Resolution No. 2016 – 39 and approved a proposed Settlement Agreement with respect to these matters. The Settlement Agreement includes a mutual waiver and release of existing claims, with narrow exceptions. Accordingly, we do not anticipate any potential future loss with respect to this matter.

C. *Concerning the Application for Water Rights of the Board of County Commissioners of Lake County, Colorado, in the Arkansas River and its Tributaries in Lake County*, Colorado Water District Court, Water Division 2, Case No. 98CW173.

The Applicant in this water matter sought amendments to its water rights, augmentation plan and appropriative exchange rights. The City of Salida filed a timely Statement of Opposition to the Application.

On April 19, 2016, the City Council authorized water counsel to enter into a Stipulation and Agreement in this matter with the Applicant. Accordingly, we do not anticipate a potential future loss with respect to this matter apart from any costs or fees incurred by the City to monitor implementation of the Stipulation and Agreement and any related Decree.

D. *Concerning the Application of the City of Colorado Springs, Acting through Colorado Springs Utilities, for Appropriative Rights of Substitution and Exchange, in the Arkansas River and its Tributaries in Pueblo, Fremont, El*

Paso, Chaffee Lake and Teller Counties, Colorado Water District Court, Water Division 2, Case No. 05CW96.

The Applicant in this water matter sought both conditional and absolute appropriative rights of exchange to divert water upstream and out-of-priority and replace it downstream with purported sources of substitute supply. The City of Salida filed a timely Statement of Opposition to the Application due to the potential impacts on 20,000 acre feet of instream flows through the City.

On April 19, 2016, the City council authorized water counsel to enter into a Stipulation and Decree in this matter with the Applicant. The City remains a party to the case for the limited purpose of ensuring that the Decree is consistent with the Stipulation and to participate in any matters of retained jurisdiction. Accordingly, we do not anticipate a potential future loss with respect to this matter apart from any costs or fees incurred by the City to monitor implementation of the Stipulation and Decree.

E. *Concerning the Application for Water Rights of City of Salida, Colorado Water District Court, Water Division 2, Case No. 04CW125.*

Concerning the Application for Water Rights of Nancy Dominick and City of Salida, Colorado Water District Court, Water Division 2, Case No. 09CW131.

In these companion cases, the City is attempting to implement a viable Alternative Delivery System ("ADS") based on a 2009 Stipulation and related legal obligation. The City obligated itself to provide and maintain the ADS in exchange for the Opposer's limited 1/32 interest in the Tennessee Ditch and its associated water rights, which the Opposer historically had used to irrigate land at the end of the Ditch.

Successful implementation of the ADS has been hampered to date by technical problems and divergent party expectations. The parties therefore jointly retained a consultant to opine on ADS implementation issues, and anticipate an independent report within the month. It is possible that the report will contain a viable implementation strategy for any ADS.

It also is possible that the City will be unable to implement the ADS adequately or at least sufficiently to satisfy the Opposer and/or the City's legal obligations under the Stipulation. Moreover, it is possible that even if the City implements a viable ADS the City will retain ongoing and costly maintenance and legal monitoring obligations.

We therefore anticipate an unfavorable outcome and a significant future loss with respect to this matter. The City stipulated to ADS obligations that it may be unable to deliver, or that will be costly to implement and maintain. We therefore believe that the City's potential future loss with respect to this matter could equal the maximum amount of the Opposer's potential damages claim, *i.e.*, the entire fair market value of her property plus the Opposer's incurred costs and fees to date. In addition, the City continues to incur ongoing costs and fees for the involvement of special water counsel.

Without the benefit of an appraisal, we currently estimate the amount of the City's potential future loss to be somewhere between \$500,000.00 and \$800,000.00 and believe that there is a greater than not probability that the risk will manifest from a potential liability into a voluntary or involuntary obligation. We do not anticipate insurance coverage for any City exposure associated with this matter.

II. Unasserted Claims and Assessments.

Pursuant to the ABA Policy Statement, it would be inappropriate for us to respond to a general inquiry relating to the existence of unasserted possible claims or assessments involving the City. We can only furnish information concerning those unasserted possible claims or assessments upon which the City has specifically requested. Moreover, we cannot address the adequacy of the City's disclosures to you of any unasserted possible claims or assessments.

The City has asked us to confirm for you its understanding that when we perform legal services for the City with respect to a matter recognized to involve unasserted possible claims or assessments that may call for a financial statement disclosure and were we form a professional conclusion that the City must disclose or consider disclosure concerning such possible claims or assessments that we will advise the City and consult with the City concerning the question of such disclosure and the applicable legal requirements. We can confirm that the City's understanding is correct.

III. Unpaid Fees.

As of May 1, 2016, the City had an outstanding balance for legal services with this firm consisting entirely of unbilled costs and fees in the amount of \$16,925.92. The City did not have any balance for legal services with this firm as of December 31, 2015.

* *

Please let us know if you have any questions regarding our opinion on this matter or need anything else with respect to your efforts.

Sincerely,

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Benjamin A. Kahn

cc: Megan Rae Kahn, Esq.
Jan Schmidt