LAFCO

9335 Hazard Way • Suite 200 • San Diego, CA 92123
(858) 614-7755 • FAX (858) 614-7766

San Diego Local Agency Formation Commission

Website: www.sdlafco.org

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June 5, 2017

TO: Local Agency Formation Commission

FROM: Executive Officer
Chief, Governmental Services

SUBJECT: San Diego LAFCO East County Fire Protection Committee and Stakeholder Committee Status Report

In November 2016, the Commission received a status report on several milestones regarding the CSA No. 115 (Pepper Drive) Reorganization proposals. Additional progress has been made since the establishment of the San Diego LAFCO East County Fire Protection Committee last year. This temporary ad hoc committee, which is scheduled to sunset following the June 5th meeting, consists of Commissioners Vanderlaan, MacKenzie, Sprague, and Supervisor Jacob. The primary purpose of the committee has been to examine the two competing reorganization applications and assist in the review of key analytical reports. Since the November update, a series of joint meetings with the stakeholders and ad hoc committee were hosted by LAFCO staff to further discuss the proposed reorganization.

A total of three technical reports have been completed since the establishment of the ad hoc committee. These reports evaluated the financial, service, and jurisdictional ramifications associated with the proposed reorganization of CSA No. 115. The latest report, which is part two of a comprehensive independent financial analysis, projects the financial condition of both agencies' governmental activities for the next ten years. Following the June 5th LAFCO meeting, the ad hoc committee will review and comment on the third and final analytical report. A copy of the forecasted financial report is attached to this memorandum for the Commission's information. Copies of all technical reports, past agendas, supporting documents, or other additional information are available electronically on LAFCO's designated CSA No. 115 webpage:

http://sdlafco.org/Webpages/csa_115_reorg.htm

After the formation of the ad hoc committee, LAFCO staff anticipated a 9-12 month timeframe before the reorganization applications would be ready for Commission consideration. During this time, the ad hoc committee agreed to participate in approximately 4 to 6 meetings to provide valuable feedback. Now that LAFCO staff's analysis of the reorganization is nearing an end, no further ad hoc committee meetings are required. The next step is to incorporate all the analytical conclusions from each technical report into one comprehensive document for the Commission. This all-inclusive report is scheduled to be presented to the Commission later this summer. This memorandum and attached financial report are presented for the Commission's information and no action is recommended.

Respectfully submitted,

MICHAEL D. OTT
Executive Officer

JOE A. SERRANO
Chief, Governmental Services

MDO:JS:eb

Attachment

Comprehensive Independent Financial Report – Part 2 of 2

LAFCO
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(858) 614-7755 • FAX (858) 614-7766
Website: www.sdlafco.org

June 5, 2017

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TO: San Diego LAFCO East County Fire Protection Committee

FROM: Executive Officer
Chief Analyst

SUBJECT: Comprehensive Independent Financial Report – Part 2 of 2

BACKGROUND

During the past several months, San Diego LAFCO's East County Fire Protection Committee has reviewed two technical reports evaluating the past financial performance and delivery of services for the San Miguel Consolidated Fire Protection District ("San Miguel FPD") and Lakeside Fire Protection District ("Lakeside FPD") in association with the proposed reorganization of County Service Area (CSA) No. 115 – Pepper Drive. These reports were produced as part of San Diego LAFCO's effort to measure the service needs for current and future CSA No. 115 residents and identify the most logical service provider(s) on a long-term basis. While the first financial report (Part One) covered the operational performance during FY 2008/09 to FY 2014/15, the second report (Part Two) is more extensive and projects the financial condition of both agencies' overall governmental activity for the next ten years. An in-depth evaluation such as this requires an all-encompassing methodical approach. This report references the data sources, assumptions, and conclusions of the forecasted data.

Financial Analysis Assumptions & Conclusions

Based on the completion of Part Two of the comprehensive independent financial report, LAFCO staff has reached a number of preliminary conclusions. The ad hoc committee should accordingly review and comment on the below conclusions.

Data Source & Assumptions

- Three rate of change ratios were used to project the next ten years in order to produce objective and impartial conclusions: (1) two-year average, (2) six-year average, and (3) a 2% inflation rate.

- The overall governmental activity of Lakeside FPD was evaluated to accurately portray its fiscal health for the next ten years. Two primary data sources were used to develop Lakeside FPD's ten-year projections: (1) 2008-2015 audited financial statements, and (2) 2008-2017 adopted budgets. Three rate of change ratios were then applied to each scenario.

- The overall governmental activity of San Miguel FPD was evaluated to accurately portray its fiscal health for the next ten years. Unlike Lakeside FPD, San Miguel FPD requires two projection scenarios: (1) the financial forecast as a stand-alone agency following the termination of the contract with CAL FIRE and (2) the financial forecast if it had maintained the contract with CAL FIRE. Five primary data sources were used to develop San Miguel FPD's ten-year projections: (1) 2008-2015 audited financial statements, (2) 2008-2017 adopted budgets, (3) July 27, 2016 Micro Study, (4) May 16, 2016 CAL FIRE Analysis Report, and (5) January 25, 2017 Dispatch Service Comparison Report. Three rate of change ratios were then applied to each scenario.

- The July 27, 2016 Micro Study conducted by San Miguel FPD measured the financial responsibility of the District as a stand-alone agency by identifying 15 budget line items as the overall budgetary costs. In order for a more conservative and thorough evaluation, LAFCO staff considered 650 budgetary costs that could potentially be impacted by the transition to a stand-alone agency. The FY 2011/12 adopted budget was the last year the District was a stand-alone agency and was used as the base year for LAFCO staff's projections. However, since a number of duplicate and one-time costs were included in San Miguel FPD's FY 2011/12 budget, many of these costs were removed from LAFCO staff's calculations. The elimination of these costs is discussed in detail in this report.

- FY 2011/12 was the last year that San Miguel FPD was a stand-alone agency. At that time, the District had 81 active employees. For projection purposes, LAFCO staff finds that the total number of past stand-alone employees (81) is similar in quantity to the proposed total number of stand-alone employees (84) following the proposed termination of the CAL FIRE contract. Accordingly, FY 2011/12 was used as the base year to calculate all of the stand-alone fire agency expenditures.

- The total net revenue for CSA No. 115 as of FY 2015/16 is approximately $350,000. Due to the pending reorganization, potential CSA No. 115 revenues and expenditures were not included in the projections because the applications submitted by San Miguel and Lakeside FPDs are still being analyzed by LAFCO staff and no Commission action has taken place yet.

- The ad hoc committee and LAFCO staff have been exploring the merits of a jointly shared fire station between Lakeside and San Miguel FPDs rather than building two new facilities less than a mile apart for the past several months. New information continues to be submitted to LAFCO regarding potential savings and costs. Due to the pending reorganization, potential joint use facility savings and expenses were not included in the projections.

- For purposes of this report, a "self-sustaining fire agency" is a term used to describe when an agency's total governmental revenue may exceed total governmental expenditures and maintain a positive reserve fund balance each fiscal year. A positive reserve fund can be used as a benchmark to verify whether an agency has available funds to finance ongoing operations and address any unanticipated fiscal liabilities.

- A working draft of this report was distributed to San Miguel and Lakeside FPDs on March 6, 2017. Subsequent meetings and supporting documents were provided to LAFCO staff. The additional information was used to develop the following conclusions.

Conclusions

- LAFCO staff's initial evaluation of San Miguel FPD consisted of all expenditures found in the District's FY 2011/12 adopted budget. Following the March 21st meeting with San Miguel FPD representatives, several budget line items were determined to be duplicates, one-time costs, equipment and services that will not be utilized, or an anomaly to the projected budgets. As a result, these specific budget line items, totaling $4.3 million, were removed or amended from the projections.

- Under the "Reestablishment of Stand-Alone Agency Scenario (2-year Average)", San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $4.2 million would increase the reserve balance each fiscal year. Refer to *Attachment D*.

- Under the "Reestablishment of Stand-Alone Agency Scenario (6-year Average)", San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $2.8 million would increase the reserve balance each fiscal year. Refer to *Attachment E*.

- Under the "Reestablishment of Stand-Alone Agency Scenario (2% Inflation Rate)", San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $3 million would increase the reserve balance each fiscal year. Refer to *Attachment F*.

- Under the “Existing Conditions Scenario (2-year Average)”, San Miguel FPD would contract with CAL FIRE and be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected surplus of approximately $1.7 million would increase the reserve balance each fiscal year. Refer to *Attachment G*.

- Under the “Existing Conditions Scenario (6-year Average)”, San Miguel FPD would contract with CAL FIRE and not be a self-sustaining fire agency because total expenditures would exceed total revenues each fiscal year resulting in a negative net income by FY 2019/20 (Year 3). A deficit in the reserve balance is projected to occur starting in Year 6 (FY 2022/23). Refer to *Attachment H*.

- Under the “Existing Conditions Scenario (2% Inflation Rate)”, San Miguel FPD would contract with CAL FIRE and be a self-sustaining fire agency because it maintains an overall positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 5 (FY 2021/22). Refer to *Attachment I*.

- Under the “Two-year Average Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 4 (FY 2020/21). Refer to *Attachment L*.

- Under the “Six-year Average Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 3 (FY 2019/20). Refer to *Attachment M*.

- Under the “Two-percent Inflation Rate Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $848,000 would increase the reserve balance each fiscal year. Refer to *Attachment N*.

This document is the third and final of a series of technical reports highlighting the financial and operational capabilities of San Miguel Consolidated and Lakeside Fire Protection Districts. While this financial analysis provides insight regarding the potential fiscal health of both agencies, it is not meant to be the deciding factor on whether the Commission should approve or disapprove either application, but rather assist in the decision making process. The financial forecasting contained in this report requires certain assumptions which may be subject to change, or even disagreement. With several conditions subject to change, such as the potential new San Miguel FPD fire station location from a site at Pepper Drive to Bradley Avenue and the effectiveness of the 4-way fire contract approved by the County and the affected agencies, other factors may need to be considered before Commission action can take place. This report is merely intended to satisfy some of the LAFCO process requirements in accordance to Government Code Sections 56425, 56430 and 56668 for the proposed CSA No. 115 reorganization. The Districts should continue reassessing all budgetary costs, specifically non-operating expenses, to address any projected financial issues in the years to come. In summary, this report concludes that both fire agencies will generally be financially sound during the next ten years. However, due to the speculative nature of LAFCO's and the Districts' fiscal projections, plus changing conditions, these conclusions should be reexamined in the near future. Therefore, a key issue for LAFCO to consider when reviewing all of these technical reports later this summer will be whether a decision to approve the CSA No. 115 reorganization should be made or postponed, pending the passage of additional time. A detailed description of the financial forecasting for both agencies' are discussed in the following sections. As previously noted, a comprehensive summary of all technical reports will be presented to the Commission later this summer.

COMPREHENSIVE FINANCIAL REPORT

Financial forecasting is the process of making educated projections about an agency's future based on historical and current data. LAFCO staff utilized this methodology to analyze the Districts' fiscal trends and develop a projected snapshot of the agencies' financial health. The historical and current data used for this technical report includes the agencies' audited financial statements, adopted budgets, internal reports such as San Miguel FPD's July 27, 2016 Micro Study, and any other information provided by the affected agencies that could assist in quantifying the future success or pitfalls of each fire agency for the next ten years (FY 2017/18 to FY 2026/27). The results of these projections will determine if San Miguel FPD and/or Lakeside FPD will be a self-sustaining fire agency in the future. For purposes of this report, a "self-sustaining fire agency" is a condition where an agency's total governmental revenue may exceed total governmental expenditures and maintain a positive reserve fund balance each fiscal year. A positive reserve fund can be used as a benchmark to verify whether an agency has available funds to finance ongoing operations and address any unanticipated fiscal liabilities.

Assumptions

Financial forecasting helps build a framework for planning and monitoring internal operations. The variables used to produce this type of framework may include several constraints such as the context of the forecast, the availability of data, the time period to be projected, and the value of the forecast to the agency. As a result, certain assumptions were made. Please note that even with a sound framework, errors and inaccuracies may occur since it is difficult to predict the future. Major external events such as economic downturn or unanticipated expenditures may distort the analytical conclusions. With that being said the source material (i.e. audits and budget data), in conjunction with certain assumptions, allowed LAFCO staff to produce an objective forecast. Below are the four primary assumptions incorporated in LAFCO staff's financial projections.

- **Current vs. Anticipated Employees:** San Miguel FPD currently has 7 active employees based on its latest audited financial statement (ending in June 30, 2015). Due to the upcoming termination of the CAL FIRE contract and subsequent reestablishment of a stand-alone agency, the District anticipates adding 77 new employees (72 under chief rankings – firefighters, paramedics, etc.; 4 battalion chiefs and 1 division chief). The addition of the new employees will bring the overall total to 84 active employees. FY 2011/12 was the last year that San Miguel FPD was a stand-alone agency. At that time, the District had 81 active employees. For projection purposes, LAFCO staff finds that the total number of past stand-alone employees (81) in FY 2011/12 is similar in quantity to the proposed total number of stand-alone employees (84) following the termination of the CAL FIRE contract.

  As for Lakeside FPD, the District currently has 56 active employees as indicated in the adopted FY 2016/17 budget. For projection purposes, staffing will be constant for Lakeside FPD. ***Assumption:*** *FY 2011/12 will be the base year to calculate all of the stand-alone fire agency expenditures for San Miguel FPD. For projection purposes, staffing will be constant for Lakeside FPD at 56 employees and 84 employees for San Miguel FPD.*

- **Rate of Change Factor:** Financial forecasting is susceptible to market fluctuation. The drastic economic decline during the late 2000s and early 2010s greatly affected public agencies at the local level. Fortunately, this nationwide recession has since ended and local agencies have generally experienced robust growth during the last several years. As a result, it is essential to utilize a number of rate of change ratios to measure past funding variation and project an agency's financial performance for the next ten years. A rate of change is the percentage of the difference in values of a variable (in this case total revenue and expenditures) during a time period to the length of that time period (in this case comparing fiscal years). Rate of change ratios are helpful in measuring whether an agency is experiencing an increase or decrease in funds. This will help calculate future revenue and expenditure trends that may have an immediate or long-term influence and determine the direction of future budgets.

  Based on the agencies' audited financial statements from the past seven years, LAFCO staff was able to calculate the average rate of change since 2008. However, there are other methods of projecting the financial performance of an agency. The use of a steady-growth rate such as the latest United States Inflation Rate can also be applied to calculate the projected financial health of an agency at a moderate level. ***Assumption:*** *Three rate of change ratios were used to project the next ten years in order to produce an objective and impartial conclusion. The projections for San Miguel FPD and Lakeside FPD factor in the following rate of change ratios: (1) two-year average, (2) six-year average, and (3) inflation rate of 2%.*

- **CSA No. 115 revenue and expenditures:** The total net revenue for CSA No. 115 as of FY 2015/16 is approximately $350,000. The two original competing applications were eventually modified by the applicants into a single application and would split the annexation and revenues of the dissolved CSA No. 115 between San Miguel FPD and Lakeside FPD. ***Assumption:*** *A conservative projection approach was used for the pending reorganization; therefore, potential CSA No. 115 revenues and expenditures were not included in the projections.*

- **Joint Use Facility:** The ad hoc committee and LAFCO staff have been exploring the merits of a jointly shared fire station between Lakeside and San Miguel FPDs rather than building two new facilities less than a mile apart for the past several months. The review of the service analysis report prepared by LAFCO staff led to an encouraging discussion between the two applicants regarding the benefit of a joint use facility. However, new information continues to be submitted to LAFCO regarding potential savings and costs to both agencies. For example, the latest information by the County Assessor's Office has indicated that the proposed San Miguel FPD fire station on Pepper Drive was incorrectly coded as non-taxable and is now subject to property taxes going forward. This correction will cause the creation of a tax bill for that portion of 2015 for which the San Miguel FPD owned it, plus all of 2016 and until perpetuity unless annexed into the District. Thus, more information by the respective boards and the County is required before we can move forward with this alternative option. ***Assumption:*** *A conservative projection approach was used for the pending reorganization; therefore, potential joint use facility savings and expenses were not included in the projections.*

San Miguel Consolidated Fire Protection District

The first financial analysis conducted by LAFCO staff specifically focused on the agency's operational revenues and expenditures to measure the historical performance at a broad level. When forecasting the financial performance of an agency, a more in-depth approach is required. The overall governmental activity of San Miguel FPD was evaluated to accurately portray its fiscal health for the next ten years. Unlike Lakeside FPD, San Miguel FPD requires two projection scenarios: (1) the financial forecast as a stand-alone agency following the termination of the contract with CAL FIRE and (2) the financial forecast if it had maintained the contract with CAL FIRE. A total of three rate of change ratios were then applied to each scenario.

These calculated rates measure the short and long term fiscal trends of an agency. The two-year average ratio captures the most recent financial performance such as the latest influx in property tax revenue and the impacts of current spending activities. On the other hand, the six-year average accounts for historical revenue, cost fluctuation, market volatility and ultimately shows a more balanced measurement of an agency's financial performance at a broader scope. While these two averages utilize audited financial data to provide accurate estimates, these ratios are based on past and current costs (i.e. contract services) which may no longer be an expense in the future. With that in mind, other growth projection techniques can also be used. The application of a steady-growth rate such as the latest United States Inflation Rate is a more straight-forward approach which increases both revenue and expenditure projections at the same rate – in this case, an overall 2% increase. Implementation of these three ratios results in a more objective glimpse of San Miguel FPD's projected financial performance. Attachments D-I depict the financial forecast for San Miguel Consolidated Fire Protection District from FY 2017/18 (year one) to FY 2026/27 (year ten) using the two-year, six-year, and inflation rate ratios for the *Stand-Alone Agency Scenario* and *Existing Conditions Scenario*. Included in each spreadsheet are budget line items and footnotes indicating the data source. The following section summarizes each scenario conclusion.

Reestablishment of Stand-alone Agency Scenario
San Miguel Consolidated FPD is currently in the fifth year of its cooperative agreement with CAL FIRE for fire services. This contract began in December 31, 2012 and is scheduled to end on June 30, 2018. Last year, San Miguel FPD conducted a micro study illustrating the projected savings prior to approving the early termination of the cooperative agreement and subsequent transition to a stand-alone agency. A copy of the July 27, 2016 Micro Study is attached to this report (see *Attachment A*). The study indicates a $1.5 million savings if the District returns to a stand-alone agency and illustrates 15 budget line items, primarily salaries and benefits, as the main budgetary costs. In contrast, a total of 650 budgetary costs were accounted for by LAFCO staff when analyzing the last fiscal year San Miguel FPD was a stand-alone agency (FY 2011/12). For a more accurate financial forecast, LAFCO staff included the budgetary costs found in the following documents: (1) FY 2011/12 adopted budget, (2) July 27, 2016 San Miguel FPD Micro Study, (3) May 16, 2016 CAL FIRE Analysis, and (4) January 25, 2017 Dispatch Service Comparison submitted and prepared by the San Miguel FPD Board President. As part of the transition to a stand-alone agency, the San Miguel FPD Board is also considering the return to Heartland Communications Facility Authority (HCFA) for dispatching services. The Dispatch Service Comparison Report, which compares the dispatching services costs between CAL FIRE and HCFA, is attached to this report (see *Attachment B*).

Since several financial reports by San Miguel FPD and CAL FIRE capture projected one-time and long-term expenses, the accumulation of all estimated expenses identified in these reports, in conjunction with the FY 2011/12 budgetary costs, were incorporated in LAFCO staff's ten-year projections. Please note that the projected expenses featured in each stand-alone scenario are referenced in the footnotes to indicate the source of the information. Due to the complexity of the projections, LAFCO staff sent a working draft to both fire districts prior to the release of the report to the ad-hoc committee. This allowed the districts to clarify any assumptions, calculations or statements found in this report. On March 21st, a meeting was held with representatives from LAFCO and San Miguel FPD to discuss the working draft. As a result, approximately 345 budget line items were removed or amended from the projections due to duplication, one-time costs, equipment and services that will not be utilized, or anomalies to past expenditures. A discussion of the removed and amended budget line items is addressed later in the report. The following section discusses the results of the three projections under the stand-alone scenario.

Reestablishment of Stand-Alone Agency Scenario (2-year Average)
LAFCO staff calculated the rate of change from FY 2012/13 to FY 2013/14 and FY 2013/14 to FY 2014/15 to compute the average two-year rate of change for San Miguel FPD as shown in ***Table A***. As a result, on average, San Miguel FPD's total revenue increased by approximately 3% and total expenditure increase by approximately 2%. The reason for the 3% average increase in total revenue is primarily due to the rise in property tax income during the last fiscal years. The District experienced a total increase of over $1.1 million in property tax revenue from FY 2012/13 to FY 2014/15. San Miguel FPD's professional services cost has increased by over $6 million since FY 2012/13 and is the primary reason for the 2% average increase in total expenditure. The two-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Table A – Calculation of Two-Year Average Trend

	FY 2012/13 Actual	FY 2013/14 Actual	FY 2014/15 Actual	Average Rate of Change (%)
Total Revenue	$18,645,755	$19,108,585	$19,711,765	
Rate of Change (%)		*2.48%*	*3.16%*	**3%**
Total Expenditure	$17,015,053	$17,239,927	$17,795,245	
Rate of Change (%)		*1.32%*	*3.22%*	**2%**

Under this scenario, San Miguel FPD would be a self-sustaining fire agency because total revenue would exceed total expenditure and the projected surplus would increase the reserve balance each fiscal year. ***Table B*** depicts the financial performance for the next ten years based on the two-year average approach. The projection estimates an average surplus of approximately $4.2 million each year. While the projections look promising, additional scenarios should be evaluated before making any determinations of San Miguel FPD's future financial performance. Refer to *Attachment D* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table B – Reestablishment of Stand-Alone Agency Scenario (2-Year Average)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (3% increase)	$21.7 million	$22.4 million	$23.0 million	$23.7 million	$24.4 million	$25.1 million	$25.8 million	$26.6 million	$27.4 million	$28.2 million
Total Expenses (2% increase)	$20.7 million	$21.7 million	$19.3 million	$19.8 million	$19.1 million	$20.7 million	$19.9 million	$21.5 million	$20.7 million	$22.4 million
Difference (+/-)	$1.0 million	$720k	$3.7 million	$3.8 million	$5.2 million	$4.4 million	$5.9 million	$5.1 million	$6.6 million	$5.7 million
Reserve Balance	$3.9 million	$4.6 million	$8.3 million	$12.2 million	$17.4 million	$21.9 million	$27.8 million	$32.9 million	$39.6 million	$45.4 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Reestablishment of Stand-Alone Agency Scenario (6-year Average)

LAFCO staff calculated the rate of change from the last seven fiscal years (FY 2008/09 to FY 2014/15) to compute the average six-year rate of change as shown in ***Table C***. As a result, on average, San Miguel FPD's total revenue decreased by approximately 1% and total expenditure decreased by approximately 2%. The decline in benefit assessments from $2.1 million in FY 2008/09 to $687,000 in FY 2014/15 in addition to the lack of interest revenue in the past four years have contributed to the 1% average decrease in total revenue. The District also experienced an average 2% decrease in total expenditure mostly due to an overall decline in operational expenses including salaries and benefits which has declined by approximately $13.3 million since FY 2008/09. The six-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Table C – Calculation of Six-Year Average Trend

	FY 08/09 Actual	FY 09/10 Actual	FY 10/11 Actual	FY 11/12 Actual	FY 12/13 Actual	FY 13/14 Actual	FY 14/15 Actual	Average Rate of Change (%)
Total Revenue	$20.8 million	$18.8 million	$18.9 million	$20.7 million	$18.6 million	$19.1 million	$19.7 million	
Rate of Change (%)		*-9.54%*	*0.67%*	*9.18%*	*-9.95%*	*2.48%*	*3.16%*	**-1%**
Total Expenditure	$20.3 million	$18.4 million	$18.6 million	$19.6 million	$17.0 million	$17.2 million	$17.7 million	
Rate of Change (%)		-8.96%	0.70%	5.61%	-13.46%	1.32%	3.22%	**-2%**

Under this scenario, San Miguel FPD would be a self-sustaining fire agency because total revenue would exceed total expenditure and the projected surplus would increase the reserve balance each fiscal year. ***Table D*** depicts the financial performance for the next ten years based on the six-year average approach. The projection estimates an average surplus of approximately $4.2 million each year. Unlike a two-year average, a six-year average provides a better representation of an agency's overall financial performance. During the six-year average time period, San Miguel FPD was a stand-alone agency for fire service from FY 2008/09 to FY 2011/12 before contracting with CAL FIRE in December 31, 2012. Refer to *Attachment E* for a complete breakdown of the projected revenue and expenditure funds under this scenario. While the projections depict the District as financially sound in the next upcoming years, a different forecasting ratio, such as a steady-growth approach, should also be evaluated before making any determinations of San Miguel FPD's future financial performance.

Table D – Reestablishment of Stand-Alone Agency Scenario (6-Year Average)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (1% decrease)	$20.9 million	$20.7 million	$20.5 million	$20.4 million	$20.2 million	$20.0 million	$19.8 million	$19.6 million	$19.5 million	$19.3 million
Total Expenses (2% decrease)	$20.6 million	$20.8 million	$17.7 million	$17.6 million	$16.2 million	$17.0 million	$15.5 million	$16.4 million	$14.9 million	$15.9 million
Difference (+/-)	$379k	-$51k	$2.8 million	$2.7 million	$3.9 million	$2.9 million	$4.2 million	$3.2 million	$4.5 million	$3.3 million
Reserve Balance	$3.2 million	$3.2 million	$6.0 million	$8.8 million	$12.8 million	$15.7 million	$20.0 million	$23.2 million	$27.8 million	$31.1 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Reestablishment of Stand-Alone Agency Scenario (2% Inflation Rate)

An inflation rate is a measure of changing prices and expressed as a percentage. The United States Bureau of Labor Statistics calculates the nation's inflation rate on a monthly and annual basis. As of December 31, 2016, the latest inflation rate was approximately 2%. Applying a 2% inflation rate offers a steady growth for the agency with a conservative annual increase in both revenue and expenditure. The inflation rate was applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Under this scenario, San Miguel FPD would be a self-sustaining fire agency because total revenue would exceed total expenditure and the projected surplus would increase the reserve balance each fiscal year. ***Table E*** depicts the financial performance for the next ten years based on the inflation rate approach. The projection estimates an average surplus of approximately $3 million each year. Refer to *Attachment F* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table E – Reestablishment of Stand-Alone Agency Scenario (2% Inflation Rate)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (2% increase)	$21.5 million	$22.0 million	$22.4 million	$22.8 million	$23.3 million	$23.7 million	$24.2 million	$24.6 million	$25.1 million	$25.6 million
Total Expenses (2% increase)	$18.9 million	$21.7 million	$19.3 million	$19.9 million	$19.2 million	$20.7 million	$19.9 million	$21.5 million	$20.7 million	$22.4 million
Difference (+/-)	$2.5 million	$279k	$3.0 million	$2.9 million	$4.0 million	$2.9 million	$4.2 million	$3.1 million	$4.3 million	$3.1 million
Reserve Balance	$5.4 million	$5.7 million	$8.8 million	$11.7 million	$15.8 million	$18.8 million	$23.0 million	$26.2 million	$30.6 million	$33.7 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Existing Conditions Scenario

The termination of the CAL FIRE contract for fire service is scheduled to go in effect on July 13, 2017. This Board action is a result of the rising contractual cost for the delivery of fire services from CAL FIRE. In order to measure the impacts of these anticipated increase in expenditure, LAFCO staff projected the financial health of the agency under the existing conditions and continuation of the CAL FIRE contract scenario. Maintaining the existing budgetary activity allows LAFCO staff to utilize the actual costs found in the audited financial statements as benchmarks for the ten-year projections. The following section discusses the results of the three projections under the existing conditions scenario.

Existing Conditions Scenario (2-year Average)

As previously mentioned, LAFCO staff calculated the rate of change from FY 2012/13 to FY 2013/14 and FY 2013/14 to FY 2014/15 to compute the average two-year rate of change as shown in ***Table A***. As a result, on average, San Miguel FPD's total revenue increased by approximately 3% and total expenditure increased by approximately 2%. The reason for the 3% average increase in total revenue is primarily due to the rise in property tax income during the last fiscal years. The District experienced a total increase of over $1.1 million in property tax revenue from FY 2012/13 to FY 2014/15. San Miguel FPD's professional services cost has increased by over $6 million since FY 2012/13 and is the primary reason for the 2% average increase in total expenditure. The two-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Under this scenario, San Miguel FPD would be a self-sustaining fire agency because total revenue would exceed total expenditure and the projected surplus would increase the reserve balance each fiscal year. ***Table F*** depicts the financial performance for the next ten years based on the two-year average approach. The projection estimates an average surplus of approximately $1.7 million each year. While the projections look promising, the overall governmental activity shows a downward trend. This is due to the estimated 5% increase in professional services costs if the District elected to contract with CALFIRE for the upcoming years. Additional scenarios should be evaluated before making any determinations of San Miguel FPD's future financial performance. Refer to *Attachment G* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table F – Existing Conditions Scenario (2-Year Average)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (3% increase)	$21.5 million	$22.1 million	$22.8 million	$23.5 million	$24.2 million	$24.9 million	$25.7 million	$26.4 million	$27.2 million	$28.1 million
Total Expenses (2% increase)	$18.2 million	$18.2 million	$19.9 million	$21.7 million	$22.6 million	$23.6 million	$24.6 million	$25.6 million	$26.7 million	$27.9 million
Difference (+/-)	$3.2 million	$3.9 million	$2.8 million	$1.7 million	$1.5 million	$1.3 million	$1.0 million	$800k	$491k	$154k
Reserve Balance	$6.1 million	$10.1 million	$12.9 million	$14.7 million	$16.3 million	$17.6 million	$18.7 million	$19.5 million	$20.0 million	$20.2 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Existing Conditions Scenario (6-year Average)

LAFCO staff calculated the rate of change from the last seven fiscal years (FY 2008/09 to FY 2014/15) to calculate the average six-year rate of change as shown in ***Table C***. As a result, on average, San Miguel FPD's total revenue decreased by approximately 1% and total expenditure decreased by approximately 2%. The decline in benefit assessments from $2.1 million in FY 2008/09 to $687,000 in FY 2014/15 in addition to the lack of interest revenue contributed to the 1% average decrease in total revenue. The District also experienced an average 2% decrease in total expenditures greatly due to an overall decline in operational expenses including salaries and benefits which has declined by approximately $13.3 million since FY 2008/09. The six-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Under this scenario, San Miguel FPD would not be a self-sustaining fire agency because total expenditure would exceed total revenue and the projected deficit would decrease the reserve balance each fiscal year starting in FY 2019/20 (Year 3). ***Table G*** depicts the financial performance for the next ten years based on the six-year average approach. Due to the slight annual decline in revenue and the 5% annual increase in fire service costs, San Miguel FPD would experience a negative financial forecast. The projection estimates an average deficit of approximately $3 million under this scenario. Refer to *Attachment H* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table G – Existing Conditions Scenario (6-Year Average)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (1% decrease)	$19.1 million	$18.9 million	$18.7 million	$18.5 million	$18.3 million	$18.1 million	$18.0 million	$17.8 million	$17.6 million	$17.4 million
Total Expenses (2% decrease)	$17.5 million	$17.2 million	$18.8 million	$20.4 million	$21.1 million	$21.8 million	$22.7 million	$23.5 million	$24.4 million	$25.4 million
Difference (+/-)	$1.5 million	$1.6 million	-$93k	-$1.8 million	-$2.7 million	-$3.7 million	-$4.7 million	-$5.7 million	-$6.8 million	-$7.9 million
Reserve Balance	$4.4 million	$6.1 million	$6.0 million	$4.1 million	$1.4 million	-$2.2 million	-$6.9 million	-$12.7 million	-$19.5 million	-$27.5 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Existing Conditions Scenario (2% Inflation Rate)

As of December 31, 2016, the latest inflation rate was approximately 2%. Applying the inflation rate offers a steady growth for the agency with a conservative increase in both revenue and expenditure each year. The inflation was applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Under this scenario, San Miguel FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. ***Table H*** depicts the financial performance for the next ten years based on the inflation rate approach. Similar to the two-year average scenario, San Miguel FPD is projected to have a positive reserve balance in the next ten years. However, the overall governmental activity experiences a downward trend due to the estimated 5% increase in professional services if the District elects to contract with CALFIRE. By Year 5, total expenditures would exceed total revenues and the District would need to withdraw from its reserves to maintain a balanced budget. Refer to *Attachment I* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table H – Existing Conditions Scenario (2% Inflation Rate)

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (2% increase)	$20.9 million	$21.3 million	$21.7 million	$22.1 million	$22.6 million	$23.0 million	$23.5 million	$24.0 million	$24.5 million	$24.9 million
Total Expenses (2% increase)	$18.2 million	$18.2 million	$19.9 million	$21.7 million	$22.6 million	$23.6 million	$24.6 million	$25.6 million	$26.7 million	$27.9 million
Difference (+/-)	$2.6 million	$3.0 million	$1.7 million	$455k	-$21k	-$531k	-$1.0 million	-$1.6 million	-$2.2 million	-$2.9 million
Reserve Balance	$5.5 million	$8.6 million	$10.4 million	$10.8 million	$10.8 million	$10.3 million	$9.2 million	$7.5 million	$5.2 million	$2.3 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

San Miguel FPD Projection Summary

The San Miguel Consolidated Fire Protection District is currently in a unique situation. The District entered into a cooperative agreement with CAL FIRE in 2012 after facing several consecutive years of declining revenues and increased costs. The contract allowed the District to shift long-term expenses and operational responsibilities to CAL FIRE - resulting in significant annual savings. Hosaka, Rotherham & Company, the District's auditor, has stated in each audited financial statement[1] that "As a result of the transition of CAL FIRE on December 31, 2012, the District's condition is improving". The auditor also notes that the annual cooperative agreement came under budget each fiscal year from FY 2011/12 to FY 2014/15 which increased the District's reserve balance during those years. The historical governmental activity performance under the current contract illustrates the positive impact to the agency (see ***Table I***). However, the Board of Directors has recently voted to terminate the CAL FIRE contract and revert back to a stand-alone agency for fire service due to the projected rising CAL FIRE costs. The financial projections under the *Existing Conditions Scenario* prepared by LAFCO staff incorporates the anticipated rising costs and does exemplify a negative impact to the agency's long-term fiscal performance if it continues to contract with CAL FIRE for fire services. *Attachment K* provides a comparison chart which summarizes both projection scenarios (Stand-Alone vs. Existing Conditions).

[1] Auditor statement discussed in the FY 2008/09 to FY 2014/15 audits under Management's Discussion and Analysis - Factors Bearing on the District's Future.

Table I – SMCFPD Annual Governmental Activity (Surplus/Deficit) Summary

	FY 09/10	FY 10/11	FY 11/12	FY 12/13	FY 13/14	FY 14/15
				Year 1 under contract	Year 2 under contract	Year 3 under contract
Total Revenue	$18,839,015	$18,964,476	$20,705,776	$18,645,755	$19,108,585	$19,711,765
Total Expense	$18,861,845	$19,153,257	$20,371,330	$19,653,587	$17,213,135	$18,384,389
Total Govt. Activity	$(22,830)	$(188,781)	$334,446	$(1,007,832)*	$1,895,450	$1,327,376

** In FY 2012/13, the District endured a decline of approximately $1.3 million in their reserves due to the uncompensated leave payout during that year.*

While LAFCO staff agrees that the projected 5% increase in CAL FIRE costs may negatively impact San Miguel's overall financial performance if a "Not to Exceed" limit is excluded in future contracts with CAL FIRE, there are still areas of concern with the stand-alone approach as well. A micro study was conducted by the District illustrating the projected savings following the transition to a stand-alone agency. While the study indicates a $1.5 million savings if the District reestablishes its fire responsibilities, the study only focuses on 15 budget line items, primarily salaries and benefits, as their overall budgetary costs and does not include a revenue breakdown, financial projections, or any discussion of their findings. In contrast, a total of 650 budgetary costs were accounted for by LAFCO staff when analyzing the last fiscal year San Miguel FPD as a stand-alone agency (FY 2011/12). A May 16, 2016 analysis report conducted by CAL FIRE also raised questions of the missing expenditures in the micro study. Supplemental charts provided by the SMCFPD Board President justifying the contract termination were distributed to the ad hoc committee on February 6, 2017 as a result of the ongoing stakeholder meetings conducted by LAFCO staff. The three charts are attached to this report (see *Attachment J*). LAFCO staff reviewed the charts and sent a letter dated February 9, 2017 with additional questions. A meeting was also held on March 1, 2017 between representatives from San Miguel FPD and LAFCO staff to discuss the charts. A copy of LAFCO's February 9th letter and San Miguel FPD response letter dated March 1st are also included in Attachment J.

When comparing all the budgetary costs as a stand-alone agency with the historical and current revenue stream, and after reviewing the financial charts and response letter provided by San Miguel FPD, LAFCO staff did not reach the same conclusion as the Micro Study. In fact, all three of the financial forecast scenarios concluded that reestablishing the stand-alone agency would result in a negative impact to the District as early as the first year following the termination of the CAL FIRE contract. However, before finalizing this report, a working draft was sent to San Miguel FPD for comments. A meeting was subsequently held on March 21st to discuss LAFCO staff's findings. Per the District's request, several specific budget line items were excluded from the projections due to duplicates, one-time costs, equipment or services that will not be utilized or anomalies to past expenditures. As a result, approximately 235 budget line items were removed and another 110 were amended resulting in a total decrease of $4.3 million in annual costs. The following is a breakdown and summary of the revisions requested by San Miguel FPD by budget category:

	FY 17/18 (Original Projections)	FY 17/18 (Revised Projections*)	Difference ($)	Difference (%)
Salaries & Benefits	$14,936,083	$13,732,148	$(1,203,935)	-8%
Maintenance & Operations	$6,966,139	$5,042,366	$(1,923,773)	-28%
Capital Outlay	$849,778	$871,597	$21,819	3%
Reserves	$1,740,938	$535,829	$(1,205,109)	-69%
Total Govt. Expenditures	**$24,492,938**	**$20,181,940**	**$(4,310,998)**	**-18%**

Footnote: Revised projections based on San Miguel FPD's edits following the review of LAFCO's original projections provided to each District on March 6, 2017.

Salaries & Benefits Category

Based on the San Miguel FPD's last adopted budget as a stand-alone agency, LAFCO staff projected salaries and benefits to be approximately $14.9 million for FY 2017/18. However, the District reduced this category by approximately $1.2 million for several reasons including but not limited to (1) elimination of specific positions, (2) no future grant funding programs, (3) and implementation of the transitional terms of employment for returning employees.

Maintenance & Operations Category

Based on the San Miguel FPD's last adopted budget as a stand-alone agency, LAFCO staff projected maintenance and operations to be approximately $6.9 million for FY 2017/18. However, the District reduced this category by approximately $1.9 million mainly because outside consultants will be utilized and certain services and equipment will not be needed following the transition back to a stand-alone agency.

Capital Outlay Category

Based on the San Miguel FPD's last adopted budget as a stand-alone agency, LAFCO staff projected capital outlay to be approximately $849,000 for FY 2017/18. However, the District corrected the budgetary line item which resulted in an increase of approximately $21,000. Please note that capital outlay are payments made in cash or cash equivalents over a period of time for liabilities such as bonds. The two active bonds, 1990a Lease Revenue Bond and CalPERS Side Fund Refinancing Bond, are scheduled to be paid off in FY 2018/19 and FY 2019/20 respectively.

Reserves Category

Based on the San Miguel FPD's last adopted budget as a stand-alone agency, LAFCO staff projected reserves to be approximately $1.7 million for FY 2017/18. However, the District reduced this category by approximately $1.2 million mainly because the Board adopted a policy in which reserve funds will be self-sustaining and no expenditures will occur if funds are not allocated to the specific fund budget.

The projections, as currently presented, illustrate a positive forecast for San Miguel FPD. However, the District will be operating in a leaner budget in comparison to its adopted budget in FY 2011/12 as a stand-alone agency. Any increases in budgetary costs from any of the four categories listed above may affect the long-term financial performance of the agency. These findings, while educated speculations, should be strongly considered and thoroughly evaluated by the San Miguel FPD Board as the District prepares to transition from the current cooperative agreement with CAL FIRE.

Lakeside Fire Protection District

The first financial analysis conducted by LAFCO staff specifically focused on the agency's operational revenue and expenditure to measure the historical performance at a broad level. However, when forecasting the financial performance of an agency, a more in-depth approach is required. The overall governmental activity of Lakeside FPD was evaluated to accurately portray its fiscal health for the next ten years. The audited financial statements were used to calculate the three rate of change ratios and project the District's financial performance. Attachments L-N depict the financial forecast for Lakeside Fire Protection District from FY 2017/18 (year one) to FY 2026/27 (year ten) using the two-year, six-year, and inflation rate ratios. The following section summarizes each scenario conclusion.

Two-Year Average Projection Scenario

LAFCO staff calculated the rate of change from FY 2012/13 to FY 2013/14 and FY 2013/14 to FY 2014/15 to compute the average two-year rate of change as shown in ***Table J***. Focusing on the last three fiscal years, on average, Lakeside FPD's total revenue increased by approximately 0.45% and total expenditure increase by approximately 1.46%. The nominal average increase in total revenue is due to the stagnant revenue stream from property tax and special assessment combined with inconsistent revenue inflow from mitigation fees and reimbursements. Between FY 2012/13 and FY 2014/15, the District experienced an increase of approximately $223,000 in property tax and $1,650 in special assessments. The slight average increase in total expenditures is due to the latest capital outlay and accrued leave payout costs during the last fiscal years. Capital Outlay costs jumped from approximately $600,000 in FY 2012/13 to over $1.1 million in FY 2014/15. The two-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Table J – Calculation of 2-Year Average Trend

	FY 2012/13 Actual	FY 2013/14 Actual	FY 2014/15 Actual	Average Rate of Change (%)
Total Revenue	$13,294,757	$13,164,879	$13,411,466	
Rate of Change (%)		*-0.98%*	*1.87%*	**0.45%**
Total Expenditure	$13,406,081	$13,816,070	$13,797,346	
Rate of Change (%)		*3.06%*	*-0.14%*	**1.46%**

Under this scenario, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. ***Table K*** depicts the financial performance for the next ten years based on the two-year average approach. However, the nominal revenue increase on an annual basis is the primary reason why the agency may experience a financial pitfall in the upcoming years based on this scenario. Even with a low increase in total expenses, the District is projected to have a negative net income starting in Year 4 (FY 2020/21).

Based on the projections, the District may need to withdraw from its reserves to maintain a balanced budget ranging from $6,800 in FY 2020/21 to $832,000 in FY 2026/27. As the economy continues to recover the agency should experience an uptick in total property tax revenue in the next several years. Therefore, additional scenarios should be evaluated before making any determinations of Lakeside FPD's future financial performance. Refer to *Attachment L* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table K – 2-Year Average Projections

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (0.45% increase)	$13.0 million	$13.0 million	$13.1 million	$13.2 million	$13.2 million	$13.3 million	$13.3 million	$13.4 million	$13.5 million	$13.5 million
Total Expenses (1.46% increase)	$12.6 million	$12.8 million	$13.0 million	$13.2 million	$13.4 million	$13.6 million	$13.8 million	$14.0 million	$14.2 million	$14.4 million
Difference (+/-)	$372k	$248k	$121k	-$7k	-$138k	-$271k	-$408k	-$547k	-$688k	-$832k
Reserve Balance	$9.3 million	$9.5 million	$9.6 million	$9.6 million	$9.5 million	$9.2 million	$8.8 million	$8.3 million	$7.6 million	$6.8 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Six-Year Average Projection Scenario

LAFCO staff calculated the rate of change from the last seven fiscal years (FY 2008/09 to FY 2014/15) to compute the average six-year rate of change as shown in ***Table L***. Based on the last seven fiscal years, on average, Lakeside FPD's total revenue increased by approximately 0.20% and total expenditure increased by approximately 1.55%. The nominal average increase in total revenue is due to the stagnant revenue stream from property tax and special assessment combined with inconsistent revenue inflow from mitigation fees and reimbursements. The District historically has earned on average $8 million in property tax and $912,000 in special assessments each fiscal year. The slight average increase in total expenditure is due to the constant increase in services and supplies expenses and the ongoing capital outlay activities. The historical average capital outlay costs since FY 2008/09 has been approximately $2.1 million. The six-year rate of change ratio was then applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Table L – Calculation of 6-Year Average Trend

	FY 08/09 Actual	FY 09/10 Actual	FY 10/11 Actual	FY 11/12 Actual	FY 12/13 Actual	FY 13/14 Actual	FY 14/15 Actual	Average Rate of Change (%)
Total Revenue	$13.4 million	$13.9 million	$12.1 million	$13.7 million	$13.2 million	$13.1 million	$13.4 million	
Rate of Change (%)		*3.31%*	*-12.4%*	*12.85%*	*-3.42%*	*-0.98%*	*1.87%*	**0.20%**
Total Expenditure	$12.9 million	$13.4 million	$15.3 million	$16.1 million	$13.4 million	$13.8 million	$13.7 million	
Rate of Change (%)		*4.16%*	*13.69%*	*5.70%*	*-17.17%*	*3.06%*	*-0.14%*	**1.55%**

Under this scenario, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. However, total expenditures will exceed total revenues beginning in FY 2019/20. ***Table M*** depicts the financial performance for the next ten years based on the six-year average approach. Similar to the two-year average scenario, the low projected revenue stream is the primary reason why the agency may experience a financial pitfall in the upcoming years. This projected negative net income is due to expenditures exceeding revenue each year starting in Year 3 (FY 2019/20). Unless adjustments are made, the agency will continue to withdraw from its reserves on average $725,000 each year to balance the annual budgets. However, even with the negative net income, the District is projected to have a positive reserve balance of $3.3 million at Year 10 (FY 2026/27). The ongoing economic recovery should result in more property tax revenue for the District and therefore more total revenue in the next several years. Nevertheless, Lakeside FPD should consider other means to balance the projected budgets if total revenues continue this historical trend. Refer to *Attachment M* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table M – 6-Year Average Projections

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (0.20% increase)	$12.9 million	$12.9 million	$12.9 million	$13.0 million	$13.0 million	$13.0 million	$13.1 million	$13.1 million	$13.1 million	$13.1 million
Total Expenses (1.55% increase)	$12.6 million	$12.8 million	$13.0 million	$13.2 million	$13.4 million	$13.7 million	$13.9 million	$14.1 million	$14.3 million	$14.5 million
Difference (+/-)	$243k	$75k	-$95k	-$268k	-$445k	-$625k	-$808k	-$995k	-$1.1 million	-$1.3 million
Reserve Balance	$9.0 million	$9.1 million	$9.0 million	$8.7 million	$8.3 million	$7.7 million	$6.9 million	$5.9 million	$4.7 million	$3.3 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Inflation Rate Projection Scenario

As of December 31, 2016, the latest inflation rate was approximately 2%. Applying the inflation rate offers a steady growth for the agency with a conservative increase in both revenue and expenditure each year. The inflation was applied to future revenues and expenditures starting with FY 2017/18 and ending in FY 2026/27.

Under this scenario, Lakeside FPD would be a self-sustaining fire agency because total revenue would exceed total expenditure and the projected surplus would increase the reserve balance each fiscal year. ***Table N*** depicts the financial performance for the next ten years based on the inflation rate approach. The projection estimates an average surplus of approximately $848,000 each year. Refer to *Attachment N* for a complete breakdown of the projected revenue and expenditure funds under this scenario.

Table N – 2% Inflation Rate Projections

Budget Item	FY 17/18	FY 18/19	FY 19/20	FY 20/21	FY 21/22	FY 22/23	FY 23/24	FY 24/25	FY 25/26	FY 26/27
Total Revenue (2% increase)	$13.6 million	$13.9 million	$14.1 million	$14.4 million	$14.7 million	$15.0 million	$15.3 million	$15.6 million	$15.9 million	$16.2 million
Total Expenses (2% increase)	$12.8 million	$13.1 million	$13.3 million	$13.6 million	$13.9 million	$14.2 million	$14.4 million	$14.7 million	$15.0 million	$15.3 million
Difference (+/-)	$774k	$790k	$806k	$822k	$838k	$855k	$872k	$890k	$907k	$925k
Reserve Balance	$10.1 million	$10.9 million	$11.7 million	$12.5 million	$13.3 million	$14.2 million	$15.1 million	$16.0 million	$16.9 million	$17.8 million
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10

Lakeside FPD Projection Summary

Lakeside Fire Protection District has maintained a fairly stable operational budget for the past seven years. However, after reviewing the overall governmental activity, the District has experienced a constant deficit since FY 10/11 (as shown in ***Table O***). This financial decline could be due to the District's ongoing capital improvement projects such as the construction of its new headquarters. Other capital improvements, including the construction of the new fire station near CSA No. 115, have also contributed to the decline in the agency's total governmental activity. The ongoing projects have depleted the reserves by over 30% from $11.4 million (FY 2010/11) to $7.8 million (FY 2014/15).

Table O – Lakeside FPD Annual Governmental Activity (Surplus/Deficit) Summary

	FY 09/10	FY 10/11	FY 11/12	FY 12/13	FY 13/14	FY 14/15
Total Revenue	$13,927,093	$12,198,770	$13,766,022	$13,294,757	$13,164,879	$13,411,466
Total Expense	$13,468,431	$15,311,729	$16,184,867	$13,406,081	$13,816,070	$13,797,346
Total Govt. Activity	$458,662	$(3,112,959)	$(2,418,845)	$(111,324)	$(651,191)	$(385,880)

Prior to the finalization of this report, a working draft was sent to Lakeside FPD for comments. A meeting was subsequently held on April 14th to discuss LAFCO staff's findings. District staffs provided LAFCO with additional information including updated data based on the Lakeside FPD's adopted Capital Funding Plan and explanation of future retirement spending such as one-time expenses to offset specific pension costs. With such proactive measures implemented, Lakeside FPD may continue to find other alternatives to reduce short and long-term expenses. Currently, Lakeside FPD still maintains a healthy reserve balance. All three scenarios indicate that the agency will be sustainable however due to the stagnant revenue inflow; the District should consider making further adjustments in upcoming budgets to avert future financial shortfalls. Based on LAFCO staff's evaluation of the latest adopted budget (FY 2016/17), 44% of total expenditure is salary and benefits ($7.6 million), 18% is CSA No. 69 contract expenses ($3.1 million), 11% is capital outlay ($1.8 million), 15% is the remaining operating expenses ($2.5 million), and 12% is the remaining non-operating expenses ($2 million). The District should reassess theses budgetary costs, specifically non-operating expenses, to address the projected financial deficits in the years to come.

CONCLUSION

This document is one of a series of reports measuring the overall fiscal performance of San Miguel Consolidated and Lakeside Fire Protection Districts. It is meant to satisfy one of the LAFCO process requirements. The estimates described in the report were based on financial documents provided by the agency or retrieved from their respective websites. As an independent agency, LAFCO staff made certain it produced a report that was objective and informative. The following are the financial analysis conclusions that the ad hoc committee should review and comment on.

Data Source & Assumptions

- Three rate of change ratios were used to project the next ten years in order to produce objective and impartial conclusions: (1) two-year average, (2) six-year average, and (3) a 2% inflation rate.

- The overall governmental activity of Lakeside FPD was evaluated to accurately portray its fiscal health for the next ten years. Two primary data sources were used to develop Lakeside FPD's ten-year projections: (1) 2008-2015 audited financial statements, and (2) 2008-2017 adopted budgets. Three rate of change ratios were then applied to each scenario.
- The overall governmental activity of San Miguel FPD was evaluated to accurately portray its fiscal health for the next ten years. Unlike Lakeside FPD, San Miguel FPD requires two projection scenarios: (1) the financial forecast as a stand-alone agency following the termination of the contract with CAL FIRE and (2) the financial forecast if it had maintained the contract with CAL FIRE. Five primary data sources were used to develop San Miguel FPD's ten-year projections: (1) 2008-2015 audited financial statements, (2) 2008-2017 adopted budgets, (3) July 27, 2016 Micro Study, (4) May 16, 2016 CAL FIRE Analysis Report, and (5) January 25, 2017 Dispatch Service Comparison Report. Three rate of change ratios were then applied to each scenario.

- The July 27, 2016 Micro Study conducted by San Miguel FPD measured the financial responsibility of the District as a stand-alone agency by identifying 15 budget line items as the overall budgetary costs. In order for a more conservative and thorough evaluation, LAFCO staff considered 650 budgetary costs that could potentially be impacted by the transition to a stand-alone agency. The FY 2011/12 adopted budget was the last year the District was a stand-alone agency and was used as the base year for LAFCO staff's projections. However, since a number of duplicate and one-time costs were included in San Miguel FPD's FY 2011/12 budget, many of these costs were removed from LAFCO staff's calculations. The elimination of these costs is discussed in detail in this report.

- FY 2011/12 was the last year that San Miguel FPD was a stand-alone agency. At that time, the District had 81 active employees. For projection purposes, LAFCO staff finds that the total number of past stand-alone employees (81) is similar in quantity to the proposed total number of stand-alone employees (84) following the proposed termination of the CAL FIRE contract. Accordingly, FY 2011/12 was used as the base year to calculate all of the stand-alone fire agency expenditures.

- The total net revenue for CSA No. 115 as of FY 2015/16 is approximately $350,000. Due to the pending reorganization, potential CSA No. 115 revenues and expenditures were not included in the projections because the applications submitted by San Miguel and Lakeside FPDs are still being analyzed by LAFCO staff and no Commission action has taken place yet.

- The ad hoc committee and LAFCO staff have been exploring the merits of a jointly shared fire station between Lakeside and San Miguel FPDs rather than building two new facilities less than a mile apart for the past several months. New information continues to be submitted to LAFCO regarding potential savings and costs. Due to the pending reorganization, potential joint use facility savings and expenses were not included in the projections.

- For purposes of this report, a "self-sustaining fire agency" is a term used to describe when an agency's total governmental revenue may exceed total governmental expenditures and maintain a positive reserve fund balance each fiscal year. A positive reserve fund can be used as a benchmark to verify whether an agency has available funds to finance ongoing operations and address any unanticipated fiscal liabilities.

- A working draft of this report was distributed to San Miguel and Lakeside FPDs on March 6, 2017. Subsequent meetings and supporting documents were provided to LAFCO staff. The additional information was used to develop the following conclusions.

Conclusions

- LAFCO staff's initial evaluation of San Miguel FPD consisted of all expenditures found in the District's FY 2011/12 adopted budget. Following the March 21st meeting with San Miguel FPD representatives, several budget line items were determined to be duplicates, one-time costs, equipment and services that will not be utilized, or an anomaly to the projected budgets. As a result, these specific budget line items, totaling $4.3 million, were removed or amended from the projections.

- Under the "Reestablishment of Stand-Alone Agency Scenario (2-year Average)", San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $4.2 million would increase the reserve balance each fiscal year. Refer to *Attachment D*.

- Under the “Reestablishment of Stand-Alone Agency Scenario (6-year Average)”, San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $2.8 million would increase the reserve balance each fiscal year. Refer to *Attachment E*.

- Under the “Reestablishment of Stand-Alone Agency Scenario (2% Inflation Rate)”, San Miguel FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $3 million would increase the reserve balance each fiscal year. Refer to *Attachment F*.

- Under the “Existing Conditions Scenario (2-year Average)”, San Miguel FPD would contract with CAL FIRE and be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected surplus of approximately $1.7 million would increase the reserve balance each fiscal year. Refer to *Attachment G*.

- Under the “Existing Conditions Scenario (6-year Average)”, San Miguel FPD would contract with CAL FIRE and not be a self-sustaining fire agency because total expenditures would exceed total revenues each fiscal year resulting in a negative net income by FY 2019/20 (Year 3). A deficit in the reserve balance is projected to occur starting in Year 6 (FY 2022/23). Refer to *Attachment H*.

- Under the “Existing Conditions Scenario (2% Inflation Rate)”, San Miguel FPD would contract with CAL FIRE and be a self-sustaining fire agency because it maintains an overall positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 5 (FY 2021/22). Refer to *Attachment I*.

- Under the “Two-year Average Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 4 (FY 2020/21). Refer to *Attachment L*.

- Under the “Six-year Average Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because it maintains a positive reserve balance during the ten-year review. However, reserve funds would be required to balance future budgets starting in Year 3 (FY 2019/20). Refer to *Attachment M*.

- Under the “Two-percent Inflation Rate Projection Scenario”, Lakeside FPD would be a self-sustaining fire agency because total revenues would exceed total expenditures. The projected annual surplus of approximately $848,000 would increase the reserve balance each fiscal year. Refer to *Attachment N*.

This document is the third and final of a series of technical reports highlighting the financial and operational capabilities of San Miguel Consolidated and Lakeside Fire Protection Districts. While this financial analysis provides insight regarding the potential fiscal health of both agencies, it is not meant to be the deciding factor on whether the Commission should approve or disapprove either application, but rather assist in the decision making process. The financial forecasting contained in this report requires certain assumptions which may be subject to change, or even disagreement. With several conditions subject to change, such as the potential new San Miguel FPD fire station location on Bradley Avenue and the effectiveness of the 4-way fire contract approved by the County and the affected agencies, other factors may need to be considered before Commission action can take place. This report is merely intended to satisfy some of the LAFCO process requirements in accordance to Government Code Sections 56668, 56425 and 56430 for the proposed CSA No. 115 reorganization. The Districts should continue reassessing all budgetary costs, specifically non-operating expenses, to address any projected financial issues in the years to come. In summary, this report concludes that both fire agencies will be financially sound during the next ten years. However, due to the speculative nature of LAFCO's and the Districts' fiscal projections, plus changing conditions, these conclusions should be reexamined in the near future. Therefore, a key issue for LAFCO to consider when reviewing all of these technical reports later this summer will be whether a decision to approve the CSA No. 115 reorganization should be made or postponed, pending the passage of additional time. A detailed description of the financial forecasting for both agencies is discussed in the above sections. Additionally, a comprehensive summary of all technical reports will be presented to the Commission later this summer.

In the interim, this report is being presented today for committee review and comment. Comments regarding the financial analysis would be greatly appreciated and will be transmitted to the Commission.

Respectfully submitted,

MICHAEL D. OTT
Executive Officer

JOE SERRANO
Chief Analyst

MDO:JS:eb

Attachments:

San Miguel Consolidated Fire Protection District:

A. July 27, 2016 Micro Study
B. January 25, 2017 Dispatch Service Comparison Report
C. May 16, 2016 CAL FIRE Cooperative Agreement Analysis
D. Stand-alone Agency Scenario (2-year Average) Projections
E. Stand-alone Agency Scenario (6-year Average) Projections
F. Stand-alone Agency Scenario (2% Inflation Rate) Projections
G. Existing Conditions Scenario (2-year Average) Projections
H. Existing Conditions Scenario (6-year Average) Projections
I. Existing Conditions Scenario (2% Inflation Rate) Projections
J. February 6, 2016 Supplemental Chart Review & Discussion
K. Stand-alone Agency Scenario vs. Existing Conditions Scenario Comparison Chart

Lakeside Fire Protection District:

L. 2-year Average Scenario Projections
M. 6-year Average Scenario Projections
N. 2% Inflation Rate Scenario Projections

Attachments available on www.sdlafco.org

http://www.sdlafco.org/Webpages/csa_115_reorg.htm