Santa Lucia Community Services District

Projected Five Year Plan

The Santa Lucia Community Services District (the "*District*") was formed in 1998 as a special district to provide essential services within its sphere of influence, The Santa Lucia Preserve. The District's sole mission is to provide the Santa Lucia Preserve Community with services related to water, wastewater treatment and collection, road and drainage maintenance, security, transportation and advanced communications. The District may exercise additional purposes whenever the Board determines by resolution, if it is feasible, economically sound and in the Community and the wider public interest, and with approval of the local area formation commission. As a public agency, the District is governed by California State Law and in particular, Community Services District Law, Section 61600.

The District generates revenue through property related fees levied upon the approximately 320 parcels on the Santa Lucia Preserve. The fee structure is recommended by the Board and approved by the voters in a continuous five year cycle.

The financial goals of the District are to ensure the responsible management of annual operating costs and the development of an appropriate reserve fund for the replacement and improvement of the District's capital assets. Reserves are funded by an operating surplus at fiscal year-end, after depreciation and net of any capital reserves spent. Over the past 8 years, the District has funded approximately $8.6 million in capital improvements. Details' regarding the operating budget are provided on the Santa Lucia Preserve website in the Community Services District section and is also available to the public upon request.

The District is governed by an elected Board of Directors consisting of five members. Each Board member must be a registered voter within the District. The Board is supplemented with a small number of advisors. Advisors are not required to be registered voters within the District and do not participate in final decisions of the Board.

<u>Goals & Objectives of the District</u>

Of the District's objectives, the health and safety of the Preserve community is of paramount importance and of highest priority. Primary concerns in this regard are, but not limited to:

- Fire protection
- Water Supply
- Emergency Response and Communications

Each of the Districts prescribed services in one way or another has a connection and resulting effect on the proper management of the critical objectives listed above.

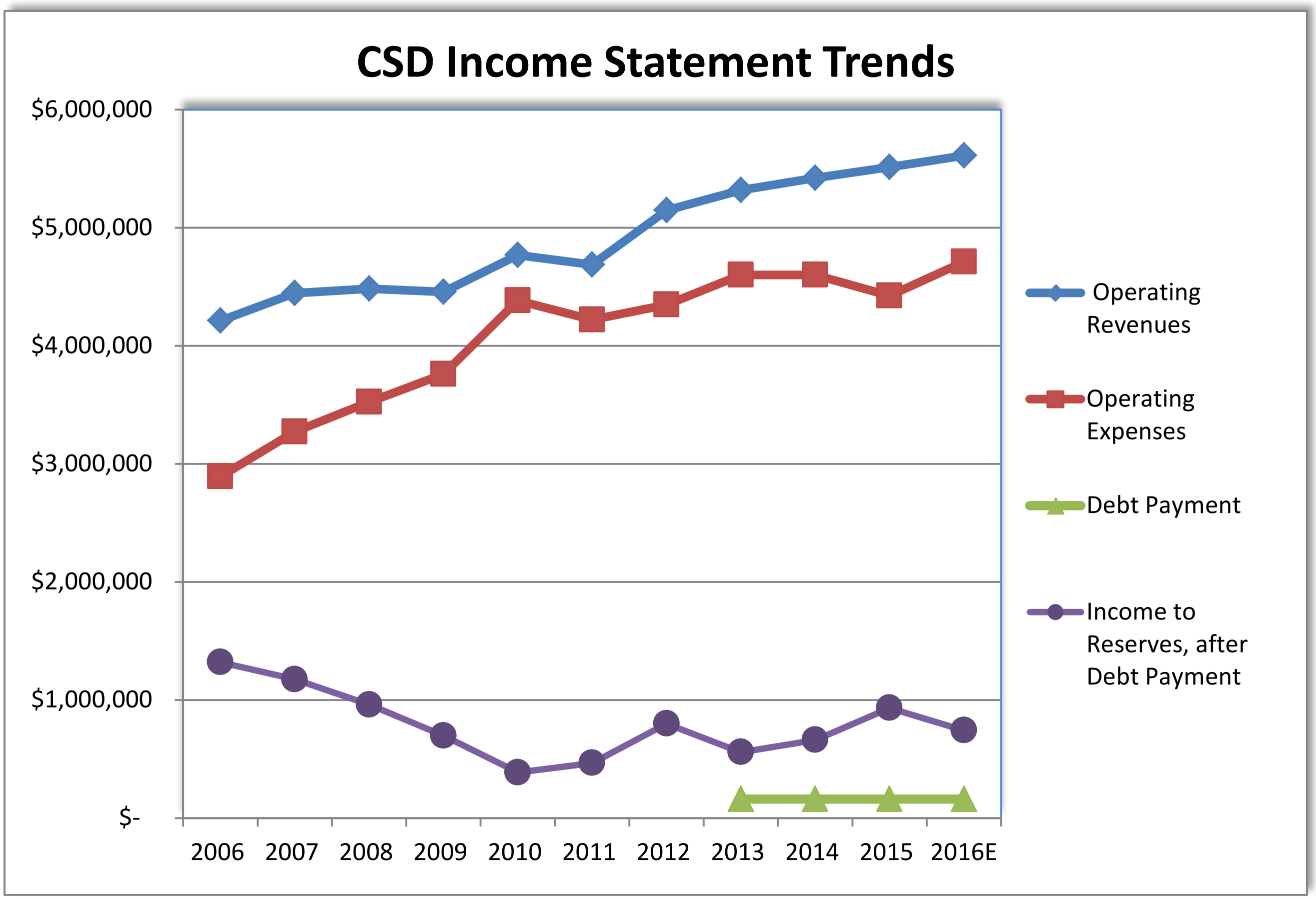
The District's goals are defined in simple terms:

- Provide required services at the highest level, while in the most cost effective and efficient manner
- Responsible management of annual operating costs and the buildup and maintenance of appropriate reserves
- The selection, training, motivation and retention of qualified men and women as service providers
- Form joint partnerships with outside agencies to ensure the highest standard of health and safety services
- Operations consistent with and supportive of the wider community goals of fire prevention, public safety and resource conservation.

The Goals and Objectives listed above drive the daily operations and management of the District. These standards are also carefully considered in the strategic planning for future years.

<u>Income Statement</u>

The following chart recaps our Income Statement over the last 11 fiscal years, including the fiscal 2016 forecast. Our fiscal year ends on June 30 and, unless otherwise noted, we refer to fiscal years.



The District operates four departments (Water, Wastewater, Roads, and Security). We maintain Net Capital Assets of $41 million and undertake significant capital projects on an ongoing basis.

We believe that our revenues should grow at the slowest rate that supports both careful expense management and adequate reserves. We have a long term goal of adding $1 million annually to our reserves. This represents funding approximately 2/3rds of our expected depreciation.

86-89% of our revenues derive from property fees/assessments. For the 5 years affecting fiscal 2012 through fiscal 2016, we asked the Community voters to approve a one-time property related fee increase of 5.7% (for turnover cost catch up) and to thereafter allow us to peg our property related fee assessments to the regional CPI. We are grateful that they did so.

In the 5 years ending fiscal 2015, our assessments increased only 18.7% over their 2010 level. The remainder of revenue is comprised of fees charged to perform work orders for other entities and usage charges, predominantly for water. Our water revenue (meter charges) grew more slowly than our assessments, in part because we asked homeowners to reduce their water use. Hence, total revenues grew only 15.6% over the 5 years.

CSD's work force of approximately 30 FTEs is spread across our 4 specialized departments. We are blessed by the experience and skill of our long serving department heads and have had modest turnover. In the years after turnover, we modestly decreased our headcount when we stopped doing work for the developer, and we more recently have increased it to meet evolving needs in the water department. We are currently at about the same FTE level as we were at turnover.

Employee-related expenses dominate our operating expenses. Approximately 55% of our operating expenses are salaries and benefits. The Preserve Company allocation, which is mostly employee-related expenses, has grown much more rapidly than our other expenses. As a percentage of operating expenses, this allocation increased from 11.5% in fiscal 2010 to 13.3% in fiscal 2015. It has run materially above budget in the first 9 months of fiscal 2016.

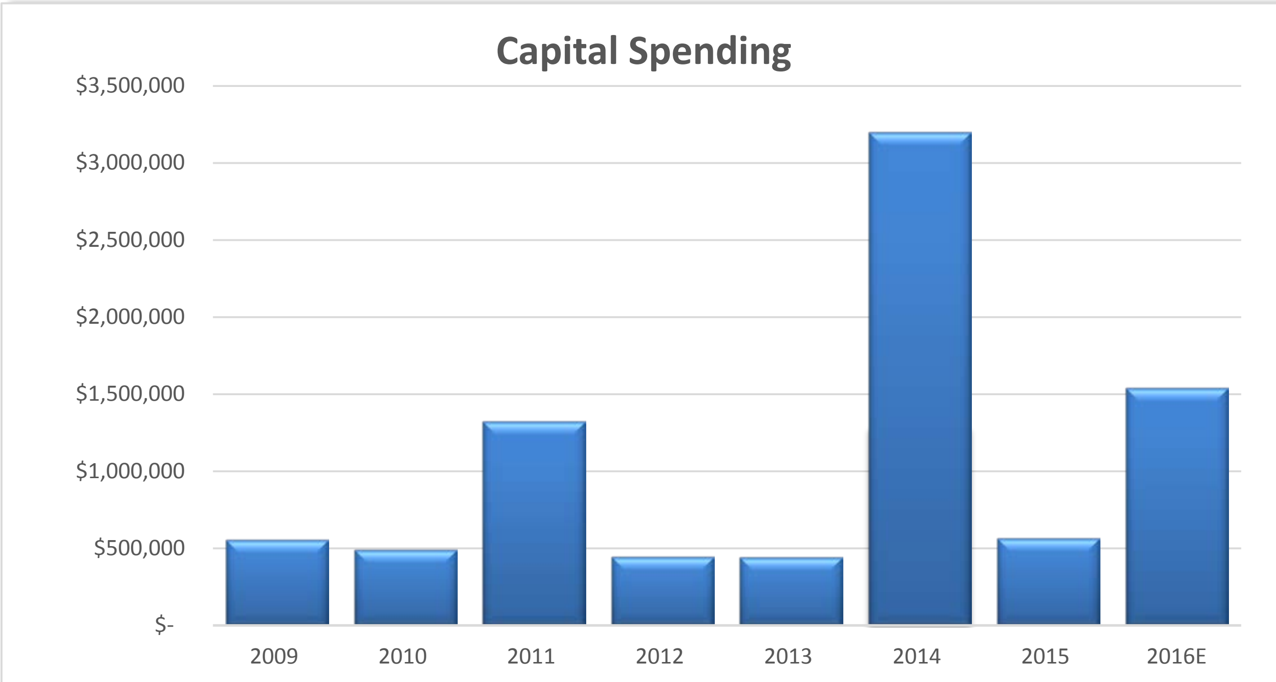
Capital Spending

Including the $1.5 million incurred in fiscal 2016, our capital spending has averaged approximately $1.1 million per year, or $8.6 million over the last 8 years. Some of this spending would have been borne by, or shared with, the Partnership, if conditions were different.

We had expected these years to be ones of significant spending. The unexpected dynamic was that we moved 3 major projects forward. The Rancho San Carlos Bridge and the sewer treatment plant both failed and we accelerated these projects. Thirdly, drought conditions led us to accelerate and expand well exploration and development. However, except for the drought, Mother Nature was relatively kind.

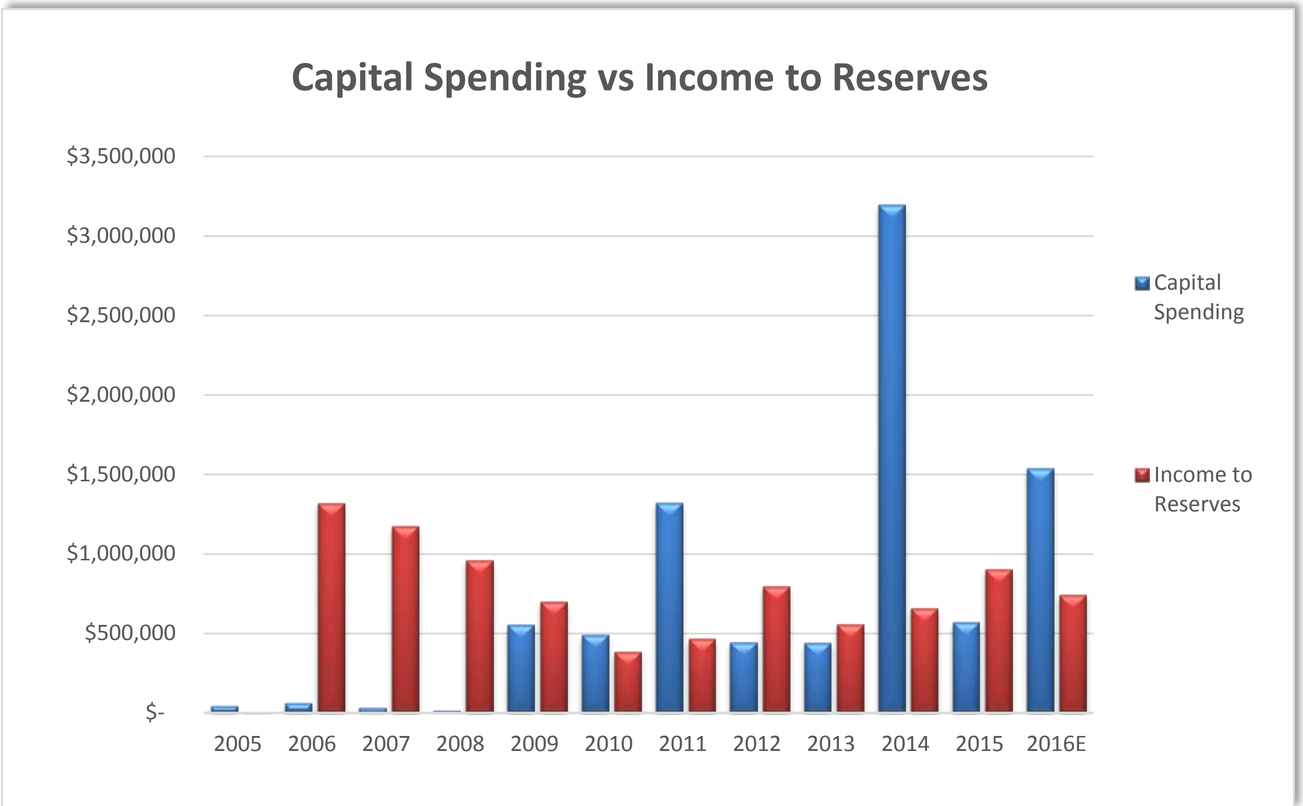
Project management was laudable. The sewer treatment plant replacement used novel technology not previously used in our State (100% low flow toilets plus torrential rain made novel technology necessary). It produced our only material cost overrun: $1.5 million versus our estimate of $1.2 million. This variance was mostly due to the drought which required us to divert our own staff and hire more expensive outside labor. We are proud of the skill and diligence of our construction managers.

The following recaps our Capital Spending.

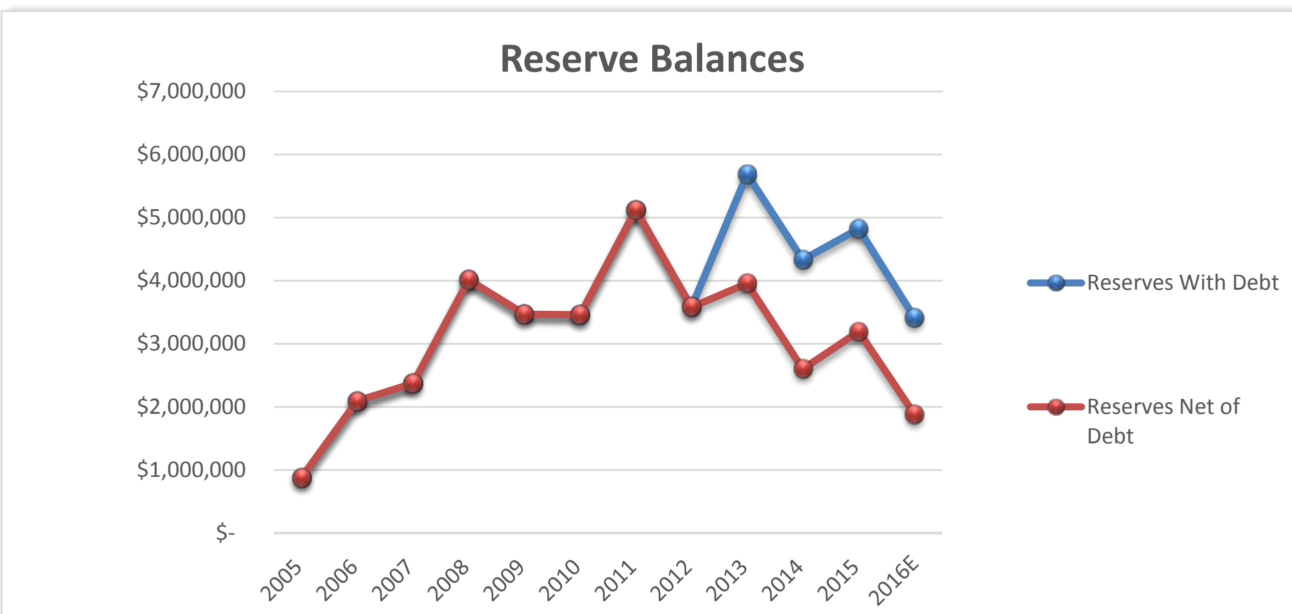


In addition to the capital spending recapped above and capitalized on our balance sheet, there are 2 noteworthy activities that affected our income statement and varied is size from year to year. In the 5 years that ended in fiscal 2016, we spent $797K on slurry repairs of our roads and, in fiscal 2014, we charged $174K in failed well development cost to our income statement.

Our goal is to contribute approximately $1 million annually to reserves. As is apparent, in recent years, we have approached, but not reached this goal, predominantly due to our employee-related expenses and our Preserve Company allocation increasing faster than inflation. The following chart recaps our Capital Spending versus Income to Reserves.



We consider our reserves to be our cash on hand. The following chart recaps our Reserve Balances (at the end of the fiscal year) and adjusts them for our outstanding long term debt.



The Increased and Increasing Cost of Water

The incremental cost of developing new water has risen and is likely to continue to rise at an accelerating rate, with respect to both operating costs and capital costs. As we look forward, we expect that water will be the biggest driver of our capital spending.

Unsurprisingly, the Partnership and CSD developed wells in locations close to our existing water treatment plants and within close proximity to utilities and existing infrastructure. These watersheds have been fully exploited. In 2014 we explored new watersheds for the first time and had our first experience drilling dry wells. Happily, we successfully drilled in a new watershed and early indications provide optimism that more water is available. As we develop this, and other new watersheds, we will need to add additional distribution and treatment facilities, requiring more capital and additional staff.

Fiscal 2016's major project was the new storage pond designated as Pond B2. It supports the Golf Club's plan to become independent of potable water. It is a comparatively cost effective way of capturing another 8 million gallons, will reduce demand pressure on aquifer ground water pumping and is in line with our conservation mission.

Fiscal 2017 through Fiscal 2021 Projections

Our projections for the upcoming five years appear on the attached Exhibit, which also shows fiscal 2012 through fiscal 2015 audited results and our fiscal 2016 forecasted results. We have asked for a property related fee assessment increase of 4% each year for the next 5 years (to begin in fiscal 2017). Our projections assume that this increase is approved by the voters.

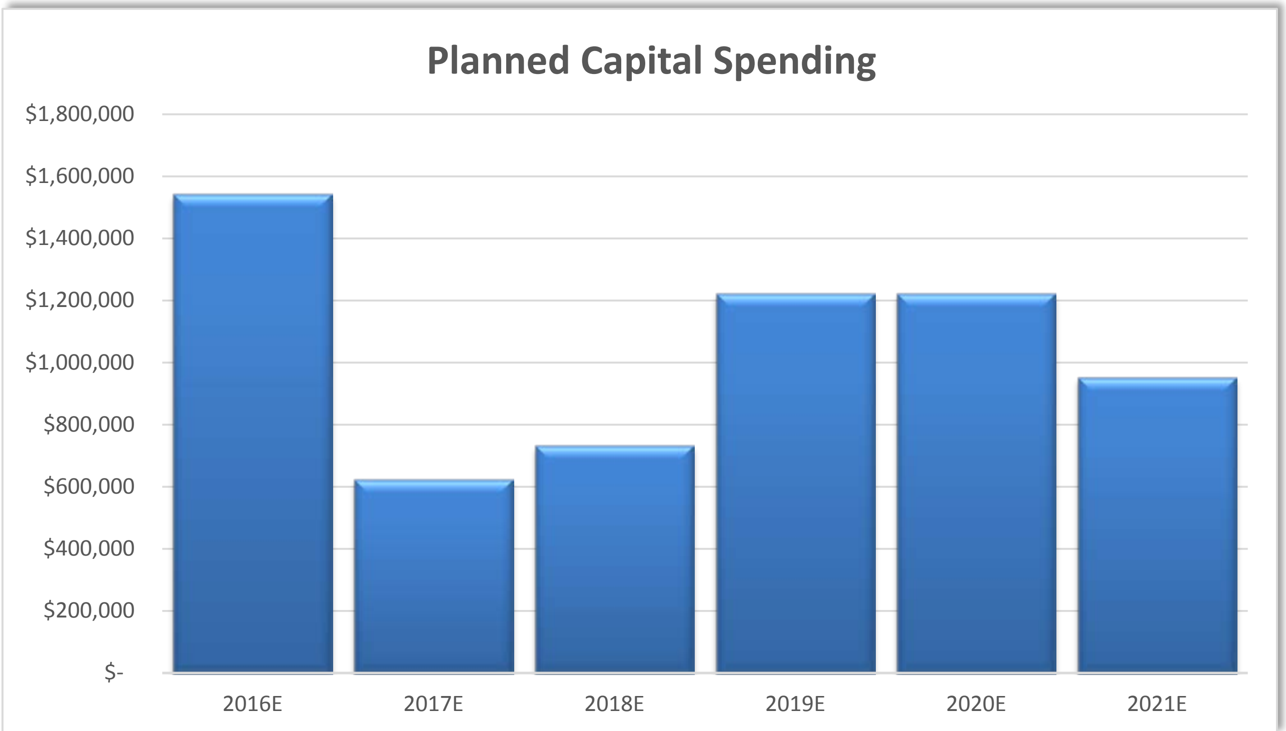
The factors underlying this plan are the following:

- In order to provide for upcoming capital spending, we need to maintain or exceed our target of a $1 million annual contribution to reserves.
- Preserve-wide salary increases have consistently exceeded the CPI. We expect this vector to continue and for its compounding effect to increase in severity since our work force is dominated by higher wage, long serving managers.
- The cost of benefits has been increasing well in excess of inflation: they are up 30% since turnover. We expect that this will continue.
- Preserve Company's allocation has grown faster than our revenues and faster than our other expenses. It is currently well above budget and we project that it will continue its rapid growth.
- We expect that our Water Department will continue to need more staff, likely when our new treatment plant comes on line.

Projected Capital Spending

Looking forward, we see that our infrastructure is aging and the cost for new water is accelerating.

Including the $1.5 million that is expected in fiscal 2016, we anticipate capital spending of $6.3 million in the six years from fiscal 2016 through fiscal 2021.



For the five years from fiscal 2017 through 2021, we estimate $4.8 million of capital spending. The large capital spending items in the fiscal 2017-2021 period are expected to be $1.7 million for water, $750K for road paving, and $750K to add a new building to the Corporation Yard to house the water department which is currently housed in Ranch Club space.

We perform road maintenance annually, depending on the degree of wear. Since 2010, this maintenance has averaged about $15oK a year. We expect to perform more significant repairs as our roads continue to age. Our projections anticipate an average of approximately $255K a year in annual road maintenance, or $1.3 million in road repair over the 5 year period.

<u>Fiber</u>

Per the suggestion of the telecommunications committee, we have spent a modest amount to obtain the authority to be a telecommunication provider in the Preserve. At a quite low cost to us, we now offer a wireless alternative from a third party vendor.

We and the telecommunications committee have negotiated a contract to install broad band infrastructure. This endeavor was exposed to the community in Town Hall meetings and has garnered strong property owner support. We have requested approval of fees to defray the cost of this project.

SANTA LUCIA PRESERVE COMPANY
Community Services District