

HIGHLANDS FIRE DISTRICT
FINANCIAL STATEMENTS
FISCAL YEAR ENDED JUNE 30, 2015
WITH REPORT OF
CERTIFIED PUBLIC ACCOUNTANTS

HIGHLANDS FIRE DISTRICT

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Independent Auditors' Report

To the Board of Directors of
Highlands Fire District

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund, of Highlands Fire District, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of Highlands Fire District, as of June 30, 2015, and the respective changes in financial position, and the respective budgetary comparison for the general fund.

Emphasis of Matter

As described in note 10 to the financial statements, the District implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and the Schedule of Funding Progress on pages 4–7 and page 32 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 19, 2015, on our consideration of the Highlands Fire District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Highlands Fire District's internal control over financial reporting and compliance.



HintonBurdick, PLLC

Flagstaff, Arizona

October 19, 2015

BOARD OF DIRECTORS

Peter Kloeber	Chair
Jan Hirsch	Clerk
William Murphy	Member
Brad Bippus	Member
Robyn Martin	Member
Dirch Foreman	Chief
Eric True	Battalion Chief
Todd Miller	Battalion Chief

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of Highlands Fire District, we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2015. Please read it in conjunction with the accompanying basic financial statements.

FINANCIAL HIGHLIGHTS

- Total assets exceed total liabilities (net position) by \$3,520,650 at the close of the fiscal year.
- Total net position decreased by \$40,357.
- Total revenues from all sources were \$4,333,382 and the total cost of all District programs was \$4,373,739.
- Total revenue received in the General Fund was \$47,640 less than the final budget and expenditures were \$248,181 less than the final budget.
- Unassigned fund balance increased \$191,273 during the fiscal year. The unassigned balance at June 30, 2015 was \$2,985,421 compared to \$2,794,148 at June 30, 2014.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The three components of the financial statements are: (1) Government-wide financial statements which include the Statement of Net Position and the Statement of Activities. These statements provide information about the activities of the District as a whole. (2) Fund financial statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the District's operations in more detail than the government-wide statements. (3) Notes to the financial statements.

Reporting the District as a Whole

The Statement of Net Position and the Statement of Activities (Government-wide)

A frequently asked question regarding the District's financial health is whether the year's activities contributed positively to the overall financial well-being. The Statement of Net Position and the Statement of Activities report information about the District as a whole and about its activities in a way that helps answer this question. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The Statement of Net Position presents financial information on all of the District's assets, liabilities, and deferred inflows/outflows of resources, with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The Statement of Activities presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported for some items that will only result in cash flows in future fiscal periods.

The Statement of Net Position and the Statement of Activities, present information about the following:

- Government activities – All of the District’s basic services are considered to be governmental activities. Property and fire assistance taxes, intergovernmental revenues and charges for services finance most of this activity.
- Proprietary activities/Business type activities – The District currently does not maintain any proprietary activities; all activities are accounted for as governmental activities.

Reporting the District’s Most Significant Funds

Fund Financial Statements

The fund financial statements provide detailed information about the most significant funds—not the District as a whole. The District’s major fund uses the accounting approaches as explained below.

- Governmental funds – All of the District’s basic services are reported in governmental funds.
Governmental funds focus on how resources flow in and out with the balances remaining at year-end that are available for spending. These funds are reported using an accounting method called the modified accrual accounting method, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the District’s general government operations and the basic services it provides. Government fund information shows whether there are more or fewer financial resources that can be spent in the near future to finance the District’s programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Position and the Statement of Activities) and governmental funds in a reconciliation included with the Basic Financial Statements and in footnote 2.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net position may serve over time as a useful indicator of the District's financial position. The District's combined assets exceed liabilities by \$3,520,650 as of June 30, 2015 as shown on the following condensed statement of net position.

	Governmental activities	
	6/30/2015	6/30/2014
Current and other assets	\$ 3,210,674	\$ 3,042,100
Capital assets	6,747,751	6,963,262
Total assets	<u>9,958,425</u>	<u>10,005,362</u>
Deferred outflows related to pensions	896,427	-
Long-term liabilities outstanding	6,629,710	3,857,959
Other liabilities	499,832	476,119
Total liabilities	<u>7,129,542</u>	<u>4,334,078</u>
Deferred inflows related to pensions	204,660	
Net position:		
Invested in capital assets, net		
of related debt	2,931,514	2,890,833
Unrestricted	589,136	2,780,451
Total net position	<u>\$ 3,520,650</u>	<u>\$ 5,671,284</u>

Governmental Activities

The cost of all Governmental activities this year was \$4,373,739. Program revenues totaled \$1,048,349 and general revenues, including taxes, investment earnings and other revenues totaled \$3,285,033.

The District's programs includes: General Government (fire protection services). Each program's revenues and expenses are presented below.

Changes in Net Position

	Governmental activities	
	6/30/2015	6/30/2014
Revenues:		
Program revenues:		
Charges for services	\$ 939,862	\$ 878,726
Operating grants and contributions	108,487	51,948
General revenues:		
Taxes	3,159,658	3,010,679
Unrestricted interest earnings	23,650	23,344
Other revenues	101,725	28,922
Total revenues	<u>4,333,382</u>	<u>3,993,619</u>
Expenses:		
Public Safety	<u>4,373,739</u>	<u>3,919,901</u>
Total expenses	<u>4,373,739</u>	<u>3,919,901</u>
Increase/(decrease) in net position	(40,357)	73,718
Net position, beginning	5,671,284	5,597,566
Restatement adjustment	(2,110,277)	-
Net position, ending	<u>\$ 3,520,650</u>	<u>\$ 5,671,284</u>

Total resources available during the year to finance governmental operations were \$7,894,389 consisting of net position at July 1, 2014 of \$5,671,284 less the restatement adjustment of \$2,110,277, program revenues of \$1,048,349 and General Revenues of \$3,285,033. Total Governmental Activities expenses during the year were \$4,373,739; thus Governmental Net Position decreased by \$40,357 to \$3,520,650.

General Fund Budgetary Highlights

The final appropriations for the General Fund at year-end were \$200,541 less than actual expenditures. Actual revenues were less than the final budget by \$47,640.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The capital assets of the District are those assets that are used in performance of District functions. Capital Assets include land, buildings and improvements, emergency vehicles, equipment and furniture and fixtures. At the end of fiscal year 2015, net capital assets of the government activities totaled \$6,747,751. Depreciation on capital assets is recognized in the Government-Wide financial statements. (See notes to the financial statements.)

Debt

At year end, the District had \$6,943,724 in governmental-type debt. This amount includes compensated absences, capital leases and net pension liability. The capital leases are secured by the land, buildings and equipment of the District. (See note 6 to the financial statements for detailed descriptions.)

NEXT YEAR'S BUDGET AND ECONOMIC FACTORS

In considering the District Budget for fiscal year 2016, the District Board and management were cautious as to the growth of revenues and expenditures. Overall General Fund operating expenditures were budgeted so as to contain costs at the same level as fiscal year 2015.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the District's finances for all those with an interest in the government's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Dirch Foreman, Chief, 2838 Kona Trail, Flagstaff, AZ 86005 or call (928) 525-1717.

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BASIC FINANCIAL STATEMENTS

HIGHLANDS FIRE DISTRICT
Statement of Net Position
June 30, 2015

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 2,976,366
Receivables	209,609
Prepaid insurance	24,699
Capital assets not being depreciated:	
Land	530,741
Capital assets, net of accumulated depreciation:	
Buildings and improvements	5,448,720
Emergency vehicles	590,275
Equipment	177,935
Furniture and fixtures	80
Total assets	9,958,425
Deferred Outflows of Resources	
Deferred outflows related to pensions	896,427
Liabilities	
Accounts payable and other current liabilities	156,805
Accrued interest payable	29,012
Noncurrent liabilities:	
Due within one year	314,015
Due in more than one year	6,629,710
Total liabilities	7,129,542
Deferred Inflows of Resources	
Deferred inflows related to pensions	204,660
Net Position	
Net investment in capital assets	2,931,514
Restricted for:	
Capital outlay	-
Public safety	-
Unrestricted	589,136
Total net position	\$ 3,520,650

The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Statement of Activities
For the Year Ended June 30, 2015

	Governmental Activities
Expenses:	
Public safety - fire protection and emergency services	\$ 3,907,209
Depreciation	307,802
Interest	158,728
Total program expenses	4,373,739
Program revenues:	
Charges for services	939,862
Operating grants and contributions	108,487
Total program revenues	1,048,349
Net program expenses	3,325,390
General revenues	
Property taxes	2,820,581
Fire District Assistance Tax (FDAT)	339,077
Unrestricted interest earnings	23,650
Gain on sale of capital assets	69,646
Other revenues	32,079
Total general revenues	3,285,033
Change in net position	(40,357)
Net position - beginning	5,671,284
Restatement adjustment	(2,110,277)
Net position - ending	\$ 3,520,650

The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Balance Sheet
Governmental Funds
June 30, 2015

	General Fund	Total Governmental Funds
Assets:		
Cash	\$ 2,976,366	\$ 2,976,366
Property tax receivables	56,070	56,070
Due from other governments	153,539	153,539
Prepaid insurance	24,699	24,699
Total Assets	3,210,674	3,210,674
Liabilities:		
Accounts payable	23,613	23,613
Accrued liabilities	133,193	133,193
Total Liabilities	156,806	156,806
Deferred Inflows of Resources		
Unavailable revenue - property taxes	43,748	43,748
Total deferred inflows of resources	43,748	43,748
Fund Balance:		
Nonspendable	24,699	24,699
Unassigned	2,985,421	2,985,421
Total Fund Balance	3,010,120	3,010,120
Total liabilities, deferred inflows of resources and fund balance	\$ 3,210,674	

Amounts reported for governmental activities in the statement of net position are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	6,747,751
Other long-term assets are not available to pay current-period expenditures and, therefore, are deferred in the funds.	43,748
Some liabilities, including capital leases and net pension liabilities, are not due and payable in the current period and therefore are not reported in the funds.	(6,280,969)
Net position of governmental activities	\$ 3,520,650

The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Statement of Revenues, Expenditures, and Changes in Fund Balance
Governmental Funds
For the Year Ended June 30, 2015

	General Fund	Total Governmental Funds
Revenues:		
Property taxes	\$ 2,818,263	\$ 2,818,263
Fire district assistance tax	339,077	339,077
Intergovernmental revenue	108,487	108,487
Charges for services	939,862	939,862
Interest income	23,650	23,650
Miscellaneous income	101,725	101,725
Total Revenues	4,331,064	4,331,064
Expenditures:		
Current:		
Salaries and wages	1,770,116	1,770,116
Wildland reimbursable wages	168,309	168,309
Employee benefits	796,622	796,622
Administration	12,190	12,190
Legal and professional	227,512	227,512
Interagency expenses	226,191	226,191
Education and training	15,828	15,828
Insurance	29,188	29,188
Dues and subscriptions	4,476	4,476
Repairs and maintenance	113,404	113,404
Supplies	98,955	98,955
Utilities	72,588	72,588
Bear Jaw operating	18,044	18,044
Cooperative assignment	17,385	17,385
Miscellaneous	3,855	3,855
Debt service:		
Principal	259,643	259,643
Interest	155,277	155,277
Capital outlay	179,961	179,961
Total Expenditures	4,169,544	4,169,544
Excess of Revenues Over (Under) Expenditures	161,520	161,520
Other financing sources (uses)		
Capital lease proceeds	-	-
Total other financing sources (uses):	-	-
Net change in fund balance	161,520	161,520
Fund Balance - Beginning of Year	2,848,600	2,848,600
Fund Balance - End of Year	\$ 3,010,120	\$ 3,010,120

The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of Governmental Funds
To the Statement of Activities
For the Year Ended June 30, 2015

Amounts reported for governmental activities in the statement of activities are different because:

Net change in fund balance - total governmental funds	\$ 161,520
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Governmental funds report capital outlays as expenditures. However, in the statement of activities, the costs of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation expense exceeded capital outlay in the current period.	(215,512)
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Accrued interest for long-term debt is not recorded as an expenditure for the current year while it is recorded in the statement of activities.	(3,450)
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The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net position. This amount is the net effect of these differences in the treatment of long-term debt and related items.	259,643
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Pension contributions are reported as expenditures in the governmental funds when made. However, they are reported as deferred outflows of resources in the Statement of Net Position because the net pension liability is measured a year before the Town's report date. Pension expense, which is the change in the net pension liability adjusted for changed in deferred outflows and inflows of resources related to pension, is reported in the Statement of Activities.	(241,285)
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Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	2,318
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Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	(3,591)
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Change in net position of governmental activities	<u>\$ (40,357)</u>
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The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Statement of Revenues, Expenditures and Changes in Fund Balance
General Fund – Budget and Actual
For the Year Ended June 30, 2015

	Budget Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		Positive (Negative)
Revenues:				
Property taxes	\$ 2,816,734	\$ 2,816,734	\$ 2,818,263	\$ 1,529
Fire district assistance tax	375,000	375,000	339,077	(35,923)
Intergovernmental revenue	161,800	161,800	108,487	(53,313)
Charges for services	989,670	989,670	939,862	(49,808)
Interest income	25,000	25,000	23,650	(1,350)
Miscellaneous income	10,500	10,500	101,725	91,225
Total Revenues	<u>4,378,704</u>	<u>4,378,704</u>	<u>4,331,064</u>	<u>(47,640)</u>
Expenditures:				
Current:				
Salaries and wages	1,895,752	1,895,752	1,770,116	125,636
Wildland reimbursable wages	150,000	150,000	168,309	(18,309)
Employee benefits	829,099	829,099	796,622	32,477
Administration	22,303	22,303	12,190	10,113
Legal and professional	213,195	213,195	227,512	(14,317)
Interagency expenses	195,000	195,000	226,191	(31,191)
Education and training	30,210	30,210	15,828	14,382
Insurance	30,330	30,330	29,188	1,142
Dues and subscriptions	4,355	4,355	4,476	(121)
Repairs and maintenance	96,615	96,615	113,404	(16,789)
Supplies	98,539	98,539	98,955	(416)
Utilities	76,700	76,700	72,588	4,112
Bear Jaw operating	34,000	34,000	18,044	15,956
Cooperative assignment	15,000	15,000	17,385	(2,385)
Miscellaneous	6,450	6,450	3,855	2,595
Debt service:				
Principal	259,643	259,643	259,643	-
Interest	139,192	139,192	155,277	(16,085)
Capital outlay	321,342	321,342	179,961	141,381
Total Expenditures	<u>4,417,725</u>	<u>4,417,725</u>	<u>4,169,544</u>	<u>248,181</u>
Excess of Revenues Over/(Under) Expenditures	<u>(39,021)</u>	<u>(39,021)</u>	<u>161,520</u>	<u>200,541</u>
Net change in fund balance	(39,021)	(39,021)	161,520	200,541
Fund Balance - Beginning of Year	<u>2,848,600</u>	<u>2,848,600</u>	<u>2,848,600</u>	<u>-</u>
Fund Balance - End of Year	<u><u>\$ 2,809,579</u></u>	<u><u>\$ 2,809,579</u></u>	<u><u>\$ 3,010,120</u></u>	<u><u>\$ 200,541</u></u>

The accompanying notes are an integral part of the financial statements.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies

Description of government-wide financial statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. All fiduciary activities are reported only in the fund financial statements. *Governmental activities*, which normally are supported by taxes, intergovernmental revenues, and other nonexchange transactions, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges to external customers for support. Likewise, when applicable, the *primary government* is reported separately from certain legally separate *component units* for which the primary government is financially accountable.

Reporting entity

Highlands Fire District (the District) was organized as a Special Service District pursuant to the provisions of Chapter 5 of Title 48 of the Arizona Revised Statutes – Special Taxing Districts, which sets forth the legal framework for a fire district. The District provides fire protection, emergency medical services, and public education programs for the communities of Kachina Village, Forest Highlands, Mountainaire, Lower Lake Mary, Pine Del, and Flagstaff Ranch Golf Club subdivision. The District is governed by an elected five member board of directors, which appoints the chairman. The District does not have any component units, meaning entities for which the District is considered to be financially accountable.

Basis of presentation – government-wide financial statements

While separate government-wide and fund financial statements are presented, they are interrelated. The governmental activities column incorporates data from governmental funds.

Basis of presentation – fund financial statements

The fund financial statements provide information about the government's funds. The emphasis of the District's fund financial statements is on major governmental funds, each is displayed in a separate column. Currently the District has only one fund, the General Fund.

The District reports the following major governmental funds:

The **General Fund** is the government's primary operating fund. It accounts for all financial resources of the general government.

Measurement focus and basis of accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as *current financial resources* or *economic resources*. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies (Continued)

The government-wide financial statements are reported using the *economic resources measurement* focus and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The governmental fund financial statements are reported using the *current financial resources measurement* focus and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Issuance of long-term debt and acquisitions under capital leases are reported as other financing sources.

Property taxes, Fire District Assistance Taxes (FDAT), and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the government.

Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position/Fund Balance

Cash, cash equivalents, and investments

Cash includes cash on hand, demand deposits with banks and deposits with the Coconino County Treasurer. The District's policy allows for the investment of funds in time certificates of deposit with federally insured depositories and other investments as allowed by state statutes.

Inventories and prepaid items

The costs of governmental fund-type inventories are recorded as expenditures when purchased rather than when consumed. Also, the District's inventory of materials and supplies is deemed to be immaterial; thus, no provision for inventory has been made in these financial statements.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. The cost of prepaid items is recorded as an expenditure when consumed rather than when purchased.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies (Continued)

Capital Assets

Capital assets, which include land, buildings, improvements, vehicles, equipment and furniture and fixtures, are reported in the governmental activities column in the government-wide statement of net position. In accordance with GASB 34, the District has opted not to retroactively report infrastructure assets. Capital assets are defined by the District as assets with an individual cost of more than \$5,000 and an estimated useful life in excess of two years. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Depreciation of capital assets is computed and recorded by the straight-line method. Estimated useful lives of the various classes of depreciable capital assets are as follows:

Buildings and improvements	5-39 years
Vehicles and equipment	5-20 years
Furniture and fixtures	5-15 years

Deferred outflows/inflows of resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/ expenditure) until then. The government currently has one type of item which qualifies for reporting in this category. It is pension related items reported on the government-wide financial statements. See footnote 7 for more information.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The government has two types of items that qualify for reporting in this category. The item, *unavailable revenue*, is reported only in the governmental funds balance sheet. The governmental funds report unavailable revenues from only one source, property taxes. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available. The other item is pension related items reported on the government-wide financial statements. See footnote 7 for more information.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies (Continued)

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the pension plan's fiduciary net position of the Arizona State Retirement System (ASRS) and Public Safety Personnel Retirement System (PSPRS) and additions to/deductions from the plan's fiduciary net position have been determined on the same basis as they are reported by ASRS and PSPRS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Net position flow assumption

Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

Fund balance flow assumptions

Sometimes the District will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the District's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Fund balance policies

Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. The government itself can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority. The governing board is the highest level of decision-making authority for the government that can, by adoption of an ordinance prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the ordinance remains in place until a similar action is taken (the adoption of another ordinance) to remove or revise the limitation.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies (Continued)

Amounts in the assigned fund balance classification are intended to be used by the District for specific purposes but do not meet the criteria to be classified as committed. The governing board (board) has by resolution authorized the board chairman to assign fund balance. The board may also assign fund balance as it does when appropriating fund balance to cover a gap between estimated revenue and appropriations in the subsequent year's appropriated budget. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or revise a commitment.

Revenues and expenditures/expenses

Program revenues

Amounts reported as program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. All taxes, including those dedicated for specific purposes, and other internally dedicated resources are reported as general revenues rather than as program revenues.

Property taxes

Property tax revenues are recognized as revenues in the year collected or if collected within 60 days thereafter unless they are prepaid.

The County levies real property taxes on or before the third Monday in August, which become due and payable in two equal installments. The first installment is due on the first day of October and becomes delinquent after the first business day of November. The second installment is due on the first day of March of the next year and becomes delinquent after the first business day of May. The County also levies various personal property taxes during the year, which are due the second Monday of the month following receipt of the tax notice and become delinquent 30 days thereafter. A lien against real and personal property assessed attaches on the first day of January preceding the assessment and levy thereof.

Compensated Absences

The District's policy permits employees to accumulate earned but unused vacation, which are eligible for payment upon separation from government service. For governmental funds, amounts of vested or accumulated vacation that are not expected to be liquidated with expendable available financial resources are reported as liabilities in the government-wide statement of net position and as expenses in the government-wide statement of activities. No expenditures are reported for these amounts in the fund financial statements.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 1. Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

New pronouncements

For the year ended June 30, 2015, the District implemented the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. GASB Statement Nos. 68 and 71 establish standards for measuring and recognizing net pension assets and liabilities, deferred outflows of resources, deferred inflows of resources, and expenses/expenditures related to pension benefits provided through defined benefit pension plans. In addition, Statement No. 68 requires disclosure of information related to pension benefits. Implementation of these new Statements resulted in a restatement of beginning net position in the District's government-wide and proprietary fund financial statements (see Note 10).

Note 2. Reconciliation of Government-Wide and Fund Financial Statements

Explanation of certain differences between the governmental fund balance sheet and government-wide statement of net position:

The governmental fund balance sheet includes a reconciliation between total governmental fund balances and net position of governmental activities as reported in the government-wide statement of net position. The differences primarily result from the long-term economic focus of the statement of net position versus the current financial resources focus of the governmental fund balance sheet.

When capital assets (property, plant and equipment) that are to be used in governmental activities are purchased or constructed, the cost of those assets are reported as expenditures in governmental funds. However, the statement of net position includes those capital assets among the assets of the District as a whole.

Cost of capital assets	\$ 10,298,429
Accumulated depreciation	<u>(3,550,678)</u>
Net adjustment to increase fund balance - total governmental funds to arrive at net position - governmental activities	<u><u>\$ 6,747,751</u></u>

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 2. Reconciliation of Government-Wide and Fund Financial Statements (Continued)

Explanation of differences between governmental fund statement of revenues, expenditures, and changes in fund balance and the government-wide statement of activities:

The governmental fund statement of revenues, expenditures, and changes in fund balance includes a reconciliation between net changes in fund balances-total governmental funds and changes in net position of governmental activities as reported in the government-wide statement of activities. The first element of this reconciliation states that capital outlays are reported in the governmental funds as expenditures while the government-wide statement of activities allocates these costs over the useful lives of the assets as depreciation. While shown in the reconciliation as the net difference, the elements of this difference are as follows:

Capital outlay	\$ 92,290
Depreciation expense	<u>(307,802)</u>
Net adjustment to decrease net changes in fund balance - total governmental funds to arrive at changes in net position - governmental activities	<u><u>\$ (215,512)</u></u>

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

NOTE 3. Stewardship, Compliance and Accountability

Budgets and Budgetary Accounting

Annual budgets are adopted on a basis consistent with GAAP for all governmental funds. Budgeted amounts are as originally adopted, or as amended by the Board.

Budgetary Process: State law requires that on or before the third Monday in July of each fiscal year, the Board must adopt a tentative budget. Once this tentative budget has been adopted, the expenditures may not be increased upon final adoption, however, they may be decreased.

Final Budget Adoption: State law specifies that exactly seven days prior to the day the property tax levy is adopted, the Board must adopt the final budget for the fiscal year. The date in State law for adoption of the tax levy is on or before the third Monday in August. The adopted budget then becomes the amount proposed for expenditure in the upcoming fiscal year. The adoption of the final budget may take place through a simple motion approved by the Board.

For management purposes, the District adopts a budget for departments within the General Fund. The Fire Chief is authorized to transfer budgeted amounts within departments; however, any revisions that alter total expenditures must be approved by the Board. Budget amendments are required to increase expenditure budgets. Expenditures may not legally exceed budgeted appropriations at the local activity level.

Expenditures over Appropriations

Expenditures may not legally exceed budgeted appropriations at the fund level. The Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual report as listed in the table of contents present expenditures/expenses over appropriations for the year ended June 30, 2015, if any.

Note 4. Deposits and Investments

Deposits as of the District at June 30, 2015 consist of the following:

Deposits:	
Cash on hand	\$ 200
Cash in bank	1,684
Cash on deposit with the Coconino County Treasurer	<u>2,974,482</u>
Total deposits	<u>\$ 2,976,366</u>

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 4. Deposits and Investments (Continued)

Deposits

Custodial Credit Risk

For deposits this is the risk that in the event of a bank failure, the government's deposit may not be returned to it. The District does not have a formal policy for custodial credit risk. As of June 30, 2015, none of the District's bank balance of \$2,546,523 was exposed to custodial credit risk because it was uninsured and uncollateralized.

The District maintains a small bank account at a local bank to facilitate electronic funds transfers of payroll liabilities to the Internal Revenue Service and employee withholdings to the Arizona State Retirement System.

Investments

The District's policy allows for the investment of funds in time certificates of deposit with federally insured depositories, investment in the county treasurer's pool, and other investments as allowed by state statutes. Eligible Arizona depositories as defined by state statutes are any commercial bank or savings and loan association with its principal place of business in the state of Arizona, which are insured by the federal deposit insurance corporation, or any other insuring instrumentality of the United States. The District had no investments as of June 30, 2015.

Interest rate risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The District's policy for managing its exposure to fair value loss arising from increasing interest rates is to comply with the state statutes which define allowable investments.

Credit risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The District's policy for reducing exposure to credit risk is to comply with the state statutes which define allowable investments.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 5. Capital Assets

The following table summarizes changes to capital assets for the year ended June 30, 2015:

Governmental Activities:	Balance 6/30/2014	Additions	Deletions	Transfers	Balance 6/30/2015
Capital assets, not being depreciated:					
Land and land improvements	\$ 530,741	\$ -	\$ -	\$ -	\$ 530,741
Total capital assets, not being depreciated	530,741	-	-	-	530,741
Capital assets, being depreciated:					
Buildings and improvements	7,061,767	-	(85,000)	-	6,976,767
Emergency vehicles	1,746,706	82,453	-	-	1,829,159
Equipment	954,873	9,837	(26,732)	-	937,978
Furniture and fixtures	23,784	-	-	-	23,784
Total capital assets, being depreciated	9,787,130	92,290	(111,732)	-	9,767,688
Less accumulated depreciation for:					
Buildings and improvements	(1,436,042)	(177,005)	85,000	-	(1,528,047)
Emergency vehicles	(1,150,723)	(88,162)	-	-	(1,238,885)
Equipment	(744,885)	(41,889)	26,732	-	(760,042)
Furniture and fixtures	(22,959)	(745)	-	-	(23,704)
Total accumulated depreciation	(3,354,609)	(307,801)	111,732	-	(3,550,678)
Total capital assets, being depreciated, net	6,963,262	(215,511)	-	-	6,747,751
Governmental activities capital assets, net	<u>\$ 6,963,262</u>	<u>\$ (215,511)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 6,747,751</u>

Depreciation expense of \$307,802 was charged to the public safety function of the District.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 6. Long-Term Debt

The following is a summary of changes in long-term debt for the year ended June 30, 2015:

Governmental Activities:	Balance 6/30/2014	Additions	Retirements	Balance 6/30/2015	Current Portion
Capital leases	\$ 4,046,868	\$ -	\$ (259,643)	\$ 3,787,225	\$ 269,714
Compensated absences	109,580	95,334	(91,744)	113,170	44,301
Net pension liabilities	2,456,674	605,041	(18,386)	3,043,329	-
Total	<u>\$ 6,613,122</u>	<u>\$ 700,375</u>	<u>\$ (369,773)</u>	<u>\$ 6,943,724</u>	<u>\$ 314,015</u>

Capital Leases

In May 2011, the District entered into a capital lease agreement with Wells Fargo Bank, N.A. as lessor to refinance the construction of a fire station facility in Forest Highlands. The new loan to Wells Fargo Bank, N.A. totaled \$1,811,850. Under the terms of the lease, semi-annual payments of \$94,173 shall be made including interest at an effective rate of 3.73 percent.

In May 2011, the District entered into a capital lease agreement with Wells Fargo Bank, N.A. as lessor to refinance the construction of a fire station facility in Mountainaire. The capital lease payable to Wells Fargo Bank, N.A. totaled \$2,883,225. Under the terms of the lease, semi-annual payments of \$104,745 shall be made including interest at an effective rate of 3.95 percent.

In May 2013, the District entered into a capital lease agreement with Kansas State Bank of Manhattan as lessor to finance the purchase of three heart monitors/defibrillators. The capital lease payable to Kansas State Bank of Manhattan totaled \$62,518. Under the terms of the lease, the first payment of \$17,085 was applied to principal; thereafter, annual payments of \$17,085 shall be made including interest at an effective rate of 6.11 percent.

A summary of the assets financed through capital leases is as follows:

	Cost	Depreciation Expense	Accumulated Depreciation
Buildings and Improvements	\$ 6,002,429	\$ 153,908	\$ 865,548
Equipment	62,518	8,931	17,862
Total	<u>\$ 6,064,947</u>	<u>\$ 162,839</u>	<u>\$ 883,410</u>

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 6. Long-Term Debt (Continued)

The following is an annual schedule of future minimum lease payments with the present value of the net minimum lease payments for the years ended June 30th:

<u>Year</u>	<u>Wells Fargo Forest Highlands</u>	<u>Wells Fargo Mountaineire</u>	<u>Kansas State Equipment</u>	<u>Total</u>
2016	\$ 188,345	\$ 209,490	\$ 17,085	\$ 414,920
2017	188,345	209,490	17,085	414,920
2018	188,345	209,490	-	397,835
2019	188,345	209,490	-	397,835
2020	188,345	209,490	-	397,835
2021-2025	563,841	1,047,449	-	1,611,290
2026-2030	-	1,047,449	-	1,047,449
2031	-	207,431	-	207,431
Total remaining lease payments	1,505,566	3,349,779	34,170	4,889,515
Less: amount representing interest	<u>(214,331)</u>	<u>(884,695)</u>	<u>(2,969)</u>	<u>(1,101,995)</u>
Present value of net remaining minimum lease payments	<u>\$ 1,291,235</u>	<u>\$ 2,465,084</u>	<u>\$ 31,201</u>	<u>\$ 3,787,520</u>

Per the lease agreements with Wells Fargo Bank, N.A., the debt of \$1,811,850 and \$2,883,225 are subject to a covenant relating to debt service. Under this covenant, the District is required to maintain a debt-coverage ratio of 1.25 on the aggregate annual debt service owed on this Credit Facility plus any other existing or future long-term obligations of the District. This ratio is measured on an annual basis and is determined by adding net excess funds, depreciation and amortization expense, and interest expense, producing an amount equivalent to Earnings Before Taxes, Depreciation, Amortization and Interest (EBITA), which is then divided by the current maturities of long-term debt plus estimated interest expense for the coming fiscal year. In addition, the non-cash pension expense that is a result of GASB 68 was added back to the earnings. See the calculation below. At June 30, 2015, the District's combined debt-coverage ratio as defined in the lease agreements were 1.60, which is in compliance with the debt covenant.

Net Income (loss) per the Statement of Activities	\$ (40,357)
Depreciation	307,802
Interest Expense	155,277
Non-cash pension expense	241,285
EBITDA	<u>\$ 664,007</u>

Interest payable on capital leases as of June 30, 2015 is \$29,012 as reported on the Statement of Net Position.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans

Arizona State Retirement System (ASRS)

Plan description – The District participates in the Arizona State Retirement System (ASRS). The ASRS administers a cost-sharing multiple-employer defined benefit pension plan, a cost-sharing multiple-employer defined benefit health insurance premium benefit (OPEB) plan, and a cost-sharing multiple-employer defined benefit long-term disability (OPEB) plan. The Arizona State Retirement System Board governs the ASRS according to the provisions of A.R.S. Title 38, Chapter 5, Articles 2 and 2.1. The ASRS issues a publicly available financial report that includes its financial statements and required supplementary information. The report is available on its website at www.azasrs.gov.

Benefits provided – The ASRS provides retirement, health insurance premium supplement, long-term disability, and survivor benefits. State statute establishes benefit terms. Retirement benefits are calculated on the basis of age, average monthly compensation, and service credit as follows:

	Initial Membership Date Before July 1, 2011	Initial Membership Date On or After July 1, 2011
Years of service and age required to receive benefit	Sum of years and age equals 80 10 years age 62 5 years age 50* any years age 65	30 years age 55 25 years age 60 10 years age 62 5 years age 50* any years age 65
Final average salary is based on	Highest 36 consecutive months of last 120 months	Highest 60 consecutive months of last 120 months
Benefit percent per year of service	2.1% to 2.3%	2.1% to 2.3%

* With actuarially reduced benefits.

Retirement benefits for members who joined the ASRS prior to September 13, 2013, are subject to automatic cost-of-living adjustments based on excess investment earning. Members with a membership date on or after September 13, 2013, are not eligible for cost-of-living adjustments. Survivor benefits are payable upon a member's death. For retired members, the survivor benefit is determined by the retirement benefit option chosen. For all other members, the beneficiary is entitled to the member's account balance that includes the member's contributions and employer's contributions, plus interest earned.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Contributions – In accordance with state statutes, annual actuarial valuations determine active member and employer contribution requirements. The combined active member and employer contribution rates are expected to finance the costs of benefits employees earn during the year, with an additional amount to finance any unfunded accrued liability. For the year ended June 30, 2015, active ASRS members were required by statute to contribute at the actuarially determined rate of 11.6 percent (11.48 percent for retirement and 0.12 percent for long-term disability) of the members' annual covered payroll, and the District was required by statute to contribute at the actuarially determined rate of 11.6 percent (10.89 percent for retirement, 0.59 percent for health insurance premium benefit, and 0.12 percent for long-term disability) of the active members' annual covered payroll.

The District's contributions for the current and two previous fiscal years were equal to the required contributions and were as follows:

Year Ended June 30,	Retirement Fund	Health Benefit Supplement Fund	Long-Term Disability Fund
2013	\$ 11,218	\$ 629	\$ 252
2014	12,070	677	271
2015	14,977	811	165

Pension liability – At June 30, 2015, the District reported a liability of \$184,220 for its proportionate share of the ASRS' net pension liability. The net pension liability was measured as of June 30, 2014. The total pension liability used to calculate the net pension liability was determined using update procedures to roll forward the total pension liability from an actuarial valuation as of June 30, 2013, to the measurement date of June 30, 2014. The District's proportion of the net pension liability was based on the District's actual contributions to the plan relative to the total of all participating employers' contributions for the year ended June 30, 2014. The District's proportion measured as of June 30, 2014, was 0.001245 percent, which was an increase of 0.000026 percent from its proportion measured as of June 30, 2013.

Pension expense and deferred outflows/inflows of resources – For the year ended June 30, 2015, the District recognized pension expense for ASRS of \$13,441. At June 30, 2015, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 9,363	\$ -
Net difference between projected and actual earnings on pension plan investments	-	32,214
Changes in proportion and differences between contributions and proportional share of contributions	3,033	-
Contributions subsequent to the measurement date	14,977	-
Total	<u>\$ 27,373</u>	<u>\$ 32,214</u>

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

The \$14,977 reported as deferred outflows of resources related to ASRS pensions resulting from District contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to ASRS pensions will be recognized in pension expense as follows:

<u>Year Ended December 31</u>	<u>Deferred Outflows (Inflows) of Resources</u>
2015	\$ (2,664)
2016	(2,664)
2017	(6,437)
2018	(8,053)
2019	
Thereafter	

Actuarial Assumptions – The significant actuarial assumptions used to measure the total pension liability are as follows:

Actuarial valuation date	June 30, 2013
Actuarial roll forward date	June 30, 2014
Actuarial cost method	Entry age normal
Investment rate of return	8%
Projected salary increases	3-6.75%
Inflation	3%
Permanent benefit increase	Included
Mortality rates	1994 GAM Scale BB

Actuarial assumptions used in the June 30, 2013, valuation were based on the results of an actuarial experience study for the 5-year period ended June 30, 2012.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

The long-term expected rate of return on ASRS pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Asset Allocation	Real Return Arithmetic Basis	Long-Term Expected Portfolio Real Rate of Return
Equity	63%	7.03%	4.43%
Fixed income	25%	3.20%	0.80%
Commodities	4%	4.50%	0.18%
Real Estate	8%	4.75%	0.38%
Totals	100%		5.79%
	Inflation		3.00%
	Expected arithmetic nominal return		8.79%

Discount Rate – The discount rate used to measure the ASRS total pension liability was 8 percent, which is less than the long-term expected rate of return of 8.79 percent. The projection of cash flows used to determine the discount rate assumed that contributions from participating employers will be made based on the actuarially determined rates based on the ASRS Board's funding policy, which establishes the contractually required rate under Arizona statute. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the proportionate share of the net pension liability to changes in the discount rate – The following table presents the District's proportionate share of the net pension liability calculated using the discount rate of 8 percent, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (7 percent) or 1 percentage point higher (9 percent) than the current rate:

	1% Decrease (7.00%)	Discount Rate (8.00%)	1% Increase (9.00%)
Proportionate share of Net pension (asset) / liability	\$ 232,844	\$ 184,220	\$ 157,838

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Pension plan fiduciary net position – Detailed information about the pension plan's fiduciary net position is available in the separately issued ASRS financial report.

Public Safety Personnel Retirement System (PSPRS)

Plan description – The District contributes to the Public Safety Personnel Retirement System (PSPRS), an agent multiple-employer defined benefit pension plan and an agent multiple-employer defined benefit health insurance premium plan that covers public safety personnel who are regularly assigned hazardous duty in the employ of the State of Arizona or a political subdivision thereof. The PSPRS, acting as a common investment administrative agent, is governed by a five-member board, known as the Fund Manager, and the participating local boards according to the provisions of A.R.S. Title 38, Chapter 5, Article 4. The PSPRS issues a publicly available financial report that includes financial statements and required supplementary information for PSPRS. That report may be obtained by writing to Public Safety Personnel, 3010 E. Camelback Road, Suite 200, Phoenix, AZ 85016 or by calling (602) 255-5575.

Benefits provided – The PSPRS provides retirement, health insurance premium supplement, disability, and survivor benefits. State statute establishes benefit terms. Retirement, disability, and survivor benefits are calculated on the basis of age, average monthly compensation, and service credit as follows:

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

	Initial Membership Date Before January 1, 2012	Initial Membership Date On or After January 1, 2012
Retirement and Disability		
Years of service and age required to receive benefit	20 years any age 15 years age 62	25 years age 52.5
Final average salary is based on	Highest 36 consecutive months of last 20 years	Highest 60 consecutive months of last 20 years months
Benefit percent		
Normal Retirement	50% less 2.0% for each year of credited service less than 20 years OR plus 2.0% to 2.5% for each year of credited service over 20 years, not to exceed 80%	2.5% per year of credited service, not to exceed 80%
Accidental Disability Retirement	50% or normal retirement, whichever is greater	
Catastrophic Disability Retirement	90% for the first 60 months then reduced to either 62.5% or normal retirement, whichever is greater	
Ordinary Disability Retirement	Normal retirement calculated with actual years of credited service or 20 years of credited service, whichever is greater, multiplied by years of credited service (not to exceed 20 years) divided by 20	
Survivor Benefit		
Retired Members	80% to 100% of retired member's pension benefit	
Active Members	80% to 100% of accidental disability retirement benefit or 100% of average monthly compensation if death was the result of injuries received on the job	

Retirement and survivor benefits are subject to automatic cost-of-living adjustments based on excess investment earnings. PSPRS also provides temporary disability benefits of 50 percent of the member's compensation for up to 12 months.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Employees covered by benefit terms – At June 30, 2015, the following employees were covered by the agent pension plans’ benefit terms:

Inactive employees or beneficiaries currently receiving benefits	5
Inactive employees entitled to but not yet receiving benefits	1
Active employees	22
Total	28

Contributions and annual OPEB cost – In accordance with state statutes, annual actuarial valuations determine active member and employer contribution requirements for pension and health insurance premium benefits. The combined active member and employer contribution rates are expected to finance the costs of benefits employees earn during the year, with an additional amount to finance any unfunded accrued liability. For the year ended June 30, 2015, active PSPSR members were required by statute to contribute 11.05 percent of their annual covered salary to the PSPRS and the District was required to contribute 41.31 percent, the remaining amounts necessary to fund the PSPRS, as determined by the actuarial basis specified by statute. The health insurance premium portion of the contribution rate was actuarially set at 1.77 percent.

For the agent plans, the District’s contributions to the pension plan and annual OPEB cost and contributions for the health insurance premium benefit for the year ended June 30, 2015, were:

Pension	
Contributions made	294,193
 Health Insurance Premium Benefit	
Annual OPEB cost	15,088
Contributions made	15,088

Pension liability – At June 30, 2015, the District reported a net pension liability of \$2,859,109. The net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The total pension liabilities as of June 30, 2014, reflect the following changes of benefit terms and actuarial assumptions.

- In February 2014, the Arizona Supreme Court affirmed a Superior Court ruling that a 2011 law changed the mechanism for funding permanent benefit increases was unconstitutional. As a result, the plans changed benefit terms to reflect the prior mechanism for funding permanent benefit increases and revised actuarial assumptions to explicitly value future permanent benefit increases.
- The wage growth actuarial assumption was decreased from 4.5 percent to 4.0 percent.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Pension actuarial assumptions – The significant actuarial assumptions used to measure the total pension liability are as follows:

Actuarial valuation date	June 30, 2014
Actuarial cost method	Individual Entry Age Normal
Discount rate	7.85%
Projected salary increases	4.0% to 8.0% including inflation
Inflation	4.0%
Permanent benefit increase	Included
Mortality rates	RP-2000 mortality table (adjusted by 105% for both males and females)

Actuarial assumptions used in the June 30, 2014, valuation were based on the results of an actuarial experience study for the 5-year period ended June 30, 2011.

The long-term expected rate of return on PSPRS pension plan investments was determined to be 7.85 using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These real rates of return are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of geometrical real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
U.S. Equity	16.00%	7.60%
Non-U.S. Equity	14.00%	8.63%
Private Equity	11.00%	9.50%
Fixed Income	7.00%	4.75%
Credit Opportunities	13.00%	8.00%
Absolute Return	4.00%	6.75%
GTAA	10.00%	5.73%
Real Assets	8.00%	5.96%
Real Estate	11.00%	6.50%
Risk Parity	4.00%	6.04%
Short Term Inv	2.00%	3.25%
Total	100.00%	

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Discount Rate –A Single Discount Rate of 7.85% was used to measure the total pension liability. This Single Discount Rate was based on the expected rate of return on pension plan investments of 7.85%. The projection of cash flows used to determine this Single Discount Rate assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on these assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Changes in the Net Pension Liability

	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability (a) - (b)
Balances at June 30, 2014	\$ 6,053,600	\$ 3,799,532	\$ 2,254,068
Changes for the year:		-	
Service cost	328,448	-	328,448
Interest on total pension liability	481,542	-	481,542
Changes of benefit terms*	70,500	-	70,500
Difference between expected and actual experience in the measurement of the pension liability	121,018	-	121,018
Changes of assumptions**	526,588	-	526,588
Contributions - employer	-	334,388	(334,388)
Contributions - employee	-	180,991	(180,991)
Net investment income	-	522,968	(522,968)
Benefit payments, including refunds of employee contributions	(167,054)	(167,054)	-
Other changes	-	(115,292)	115,292
Net changes	1,361,042	756,001	605,041
Balances at June 30, 2015	\$ 7,414,642	\$ 4,555,533	\$ 2,859,109

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Sensitivity of the proportionate share of the net pension liability to changes in the discount rate – The following table presents the District's net pension liability calculated using the discount rate noted above, as well as what the District's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

	1% Decrease (6.85%)	Discount Rate (7.85%)	1% Increase (8.85%)
Proportionate share of Net pension (asset) / liability	\$ 3,899,620	\$ 2,859,109	\$ 1,999,131

Pension plan fiduciary net position – Detailed information about the pension plan's fiduciary net position is available in the separately issued PSPRS financial report.

Pension expense and deferred outflows/inflows of resources – For the year ended June 30, 2015, the District recognized pension expense for PSPRS of \$537,014. At June 30, 2015, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 107,424	\$ -
Changes in assumptions	467,437	-
Net difference between projected and actual earnings on	-	172,446
Contributions subsequent to the measurement date	294,193	-
Total	\$ 869,054	\$ 172,446

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

The \$294,193 reported as deferred outflows of resources related to PSPRS pensions resulting from District contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to PSPRS pensions will be recognized in pension expense as follows:

<u>Year Ended December 31</u>	<u>Outflows (Inflows) of Resources</u>
2015	\$ 29,633
2016	29,633
2017	29,633
2018	29,633
2019	72,745
Thereafter	211,138

Agent plan OPEB actuarial assumptions – The health insurance premium benefit contribution requirements for the year ended June 30, 2015, were established by the June 30, 2013, actuarial valuations, and those actuarial valuations were based on the following actuarial methods and assumptions.

Actuarial valuations involve estimates of the reported amounts' value and assumptions about the probability of events in the future. Amounts determined regarding the plans' funded status and the annual required contributions are subject to continual revision as actual results are compared to past expectations and new estimates are made. The required schedule of funding progress for the health insurance premium benefit presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of the plans' assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Projections of benefits are based on (1) the plan as the District and plans' members understand them and include the types of benefits in force at the valuation date, and (2) the pattern of sharing benefit costs between the District and plans' members to that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. The significant actuarial methods and assumptions used are the same for all PSPRS plans and related benefits (unless noted), and the following actuarial methods and assumptions were used to establish the fiscal year 2015 contribution requirements:

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Actuarial valuation date	June 30, 2013
Actuarial cost method	Individual Entry Age Normal
Amortization Method	Level Percentage of Pay, Closed
Remaining Amortization Period	23 years for unfunded liabilities; 20 years for excess
Asset valuation method	7-Year smoothed market; 20% corridor
Actuarial assumptions:	
Investment rate of return	7.85%
Projected salary increases	4.5%-8.5%
Wage growth	4.50%

Agent plan OPEB trend information – Annual OPEB cost information for the health insurance premium benefit for the current and 2 preceding years follows:

Plan	Year Ended June 30,	Annual Pension/ OPEB Cost	Percentage of Annual Cost Contributed	Net Pension/ OPEB Obligation
Health Insurance	2013	\$ 13,339	100%	-
	2014	13,200	100%	-
	2015	15,088	100%	-

Agent plan OPEB funded status – The health insurance premium benefit plans’ funded status as of the most recent valuation date, June 30, 2014, along with the actuarial assumptions and methods used in those valuations follow.

	<u>Insurance Subsidy</u>
Actuarial accrued liability (AAL)	\$ 153,585
Actuarial value of plan assets	<u>146,045</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 7,540</u>
Funded ratio (actuarial value of plan assets/AAL)	95.09%
Covered payroll (active plan members)	\$ 1,658,989
UAAL as a percentage of covered payroll	0.45%

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 7. Retirement and Pension Plans (Continued)

Actuarial valuation date	June 30, 2014
Actuarial cost method	Individual Entry Age Normal
Amortization Method	Level Percentage of Pay, Closed
Remaining Amortization Period	22 years for unfunded liabilities; 20 years for excess
Asset valuation method	7-Year smoothed market; 20% corridor
Actuarial assumptions:	
Investment rate of return	7.85%
Projected salary increases	4.0%-8.0%
Wage growth	4.0%

Volunteer Pension Fund

Description of Plan - Highlands Fire District adopted an Article 4 Alternate Pension and Benefit Plan, a defined contribution plan, for the benefit of its volunteer firefighting staff on June 26, 2000. The Plan is administered by The Innes Associates, Ltd. The Plan provides retirement benefits to volunteer employees on an awarded number of units method based on performance evaluation results. The Innes Associates, Ltd. issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to The Innes Associates, Ltd., 2425 E. Camelback Road, Suite 950, Phoenix, AZ 85016.

Funding policy - In May 2004, Highlands Fire District's Board of Directors approved the adoption of a contribution policy based on a service oriented formula. This formula takes into account core competency, responses to emergencies, participation and standards evaluations. For each plan year, the District shall make a contribution out of the General Fund to the Plan in an amount determined by the Board of Directors according to this formula.

The Volunteer Pension Fund is presently self-sustaining due to the build-up of a large unallocated reserve produced by forfeitures. This reserve is being used to fund current volunteer pension contributions based on the service oriented formula and will be so used until it is depleted in its entirety.

The Volunteer Pension Fund was terminated effective June 30, 2015.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

Note 8. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets and natural disasters. The District has insurance protection and the limit for basic coverage is for \$1,000,000 per occurrence on a claims made basis. No significant reduction in insurance coverage occurred during the year and no settlements exceeded insurance coverage during any of the past three fiscal years.

Note 9. Intergovernmental Agreements

On April 25, 2012, the District entered into an agreement with Flagstaff Ranch Fire District (Flagstaff Ranch) for around the clock fire and emergency medical services provided by the District for the residents and property owners of the Flagstaff Ranch Golf Club subdivision beginning on July 1, 2012. The agreement calls for an annual fee of \$110,000, which is receivable in twelve monthly installments and will expire on June 30, 2015 with the option to renew for two additional years. This agreement was renewed for the fiscal year ending June 30, 2016. Flagstaff Ranch further agrees to pay the District at the rate of \$1,000 per hour for any emergency incident which exceeds three hours in duration retroactive to the time the initial call for service was received.

On August 23, 2010, the District entered into an agreement with Pinewood Fire District (Pinewood) and Summit Fire District (Summit) for the purpose of establishing, operating and managing the interagency fire crew known as the Bear Jaw Fire and Fuels Module (Module). The purpose of the Module is to perform all aspects of hazard fuel mitigation, primarily thinning and burning, public education and wildfire suppression across the partner agency's jurisdictions. Per the agreement, the District is assigned with the tasks of maintaining the annual budget, performing needed invoicing, collecting funds, reporting grant reimbursements and distributing funds to Pinewood and Summit. The District, Pinewood and Summit shall equally share the cost of operating supplies and Americorps positions in the event that insufficient revenue is generated to cover these costs. The agreement may be terminated by any party upon thirty days written notice to the other parties.

HIGHLANDS FIRE DISTRICT
Notes to the Financial Statements
June 30, 2015

NOTE 10. Restatement Adjustment

As mentioned in Note 1 to the financial statements, the District implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, as amended by GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. GASB Statement Nos. 68 and 71 establish standards for measuring and recognizing net pension assets and liabilities, deferred outflows of resources, deferred inflows of resources, and expenses/expenditures related to pension benefits provided through defined benefit pension plans. This resulted in a restatement of beginning net position as follows:

	<u>Governmental Activities</u>
Restatement adjustment - implementation of GASB 68:	
Net pension liability	\$ (2,456,674)
Deferred outflows - contributions made during fiscal year 2014	<u>346,397</u>
Total Restatement Adjustment	<u><u>\$ (2,110,277)</u></u>

Required Supplementary Information

HIGHLANDS FIRE DISTRICT
Schedule of the Proportionate Share of the Net Pension Liability
June 30, 2015

Arizona State Retirement System

	Reporting Fiscal Year (Measurement Date)	
	2015 (2014)	
Proportion of the net pension liability (asset)		0.001219%
Proportionate share of the net pension liability (asset)	\$	184,220
Covered employee payroll	\$	127,328
Proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll		144.68%
Plan fiduciary net position as a percentage of the total pension liability		69.49%

Note: The District implemented GASB 68 in fiscal year 2015. Information prior to 2015 is not available.

HIGHLANDS FIRE DISTRICT
Schedule of Contributions
June 30, 2015

Arizona State Retirement System

	Reporting Fiscal Year (Measurement Date)	
	2015	(2014)
Contractually required contribution	\$	12,009
Contributions in relation to the contractually required contribution	\$	(12,009)
Contribution deficiency (excess)	\$	-
Covered employee payroll	\$	127,328
Contributions as a percentage of covered-employee payroll		9.43%

Note: The District implemented GASB 68 in fiscal year 2015. Information prior to 2015 is not available.

HIGHLANDS FIRE DISTRICT
Schedule of Changes in the Net Pension Liability and Related Ratios
June 30, 2015

Public Safety Personnel Retirement System

	Reporting Fiscal Year
	(Measurement Date)
	2015
	(2014)
Total pension liability	
Service cost	\$ 328,448
Interest on total pension liability	481,542
Changes of benefit terms*	70,500
Difference between expected and actual experience of the total net pension liability	121,018
Changes of assumptions	526,588
Benefit payments, including refunds of employee contributions	(167,054)
Net change in total pension liability	1,361,042
Total pension liability - beginning	6,053,600
Total pension liability - ending (a)	\$ 7,414,642
 Plan fiduciary net position	
Contributions - employer	\$ 334,388
Contributions - employee	180,991
Net investment income	522,968
Benefit payments, including refunds of employee contributions	(167,054)
Other (net transfer)	(115,292)
Net change in plan fiduciary net position	756,001
Plan fiduciary net position - beginning	3,799,532
Plan fiduciary net position - ending (b)	\$ 4,555,533
 Net pension liability - ending (a) - (b)	\$ 2,859,109
 Plan fiduciary net position as a percentage of the total pension liability	61.44%
 Covered employee payroll	\$ 1,800,163
 Net pension liability as a percentage of covered-employee payroll	158.83%

Note: The District implemented GASB 68 in fiscal year 2015. Information prior to 2015 is not available.

HIGHLANDS FIRE DISTRICT
Schedule of Contributions
June 30, 2015

Public Safety Personnel Retirement System

	Reporting Fiscal Year
	(Measurement Date)
	2015
	(2014)
Actuarially determined contribution	\$ 334,388
Contributions in relation to the actuarially determined contribution	\$ (334,388)
Contribution deficiency (excess)	\$ -
Covered-employee payroll	\$ 1,800,163
Contributions as a percentage of covered-employee payroll	18.58%

Note: The District implemented GASB 68 in fiscal year 2015. Information prior to 2015 is not available.

HIGHLANDS FIRE DISTRICT
Required Supplementary Information
Schedule of Agent OPEB Plan Funding Progress
June 30, 2015

Public Safety Personnel Retirement System						
Health Insurance Premium Benefit						
	(a)	(b)	(b) - (a)	(a)/(b)	(c)	Unfunded AAL As a Percentage of Covered Payroll [(b)-(a)] / (c)
Valuation Date June 30,	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Annual Covered Payroll	
2012	-	134,783	134,783	0.0%	1,662,865	8.11%
2013	-	150,179	150,179	0.0%	1,664,640	9.02%
2014	146,045	153,585	7,540	95.09%	1,658,989	0.45%
2015	**	**	**	**	**	**

HIGHLANDS FIRE DISTRICT
Required Supplementary Information
Notes to Pension Plan Schedules
June 30, 2015

NOTE 1. Actuarially Determined Contribution Rates

Actuarially determined contribution rates for PSPRS are calculated as of June 30 two years prior to the end of the fiscal year in which contributions are made. The actuarial methods and assumptions used to establish the contribution requirements are as follows:

Actuarial cost method	Individual Entry Age Normal
Amortization Method	Level Percentage of Payroll, Closed
Remaining Amortization Period	24 years for unfunded liabilities; 20 years for excess
Asset valuation method	7-Year smoothed market; 20% corridor
Actuarial assumptions:	
Investment rate of return	In the 2014 actuarial valuation, the investment rate of return was decreased from 8.0% to 7.85%
Projected salary increases	In the 2014 actuarial valuation, the projected salary increases were decreased from 5.0%-9.0% to 4.0%-8.0%
Wage growth	In the 2014 actuarial valuation, wage growth was decreased from 5.0% to 4.0%
Retirement age	Experience-based table of rates that is specific to the type of eligibility condition. Last updated for the 2012 valuation pursuant to an experience study of the period July 1, 2006 - June 30, 2011.
Mortality	RP-2000 mortality table projected to 2015 using projection scale AA (adjusted by 105% for both males and females)

NOTE 2. Factors that Affect the Identification of Trends

Beginning in fiscal year 2014, PSPRS established separate funds for pension benefits and health insurance premium benefits. Previously, the plans recorded both pension and health insurance premium contributions in the same Pension Fund. During fiscal year 2014, the plans transferred prior-year health insurance premium benefit contributions that exceeded benefit payments from each plan's Pension Fund to the new Health Insurance Fund.

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Other Communications from Independent Auditors

**Independent Auditors' Report on Internal Control
Over Financial Reporting and on Compliance and other
Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards***

To the Board of Directors of
Highlands Fire District

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities and each major fund of Highlands Fire District, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise Highlands Fire District's basic financial statements, and have issued our report thereon dated October 19, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Highland Fire District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Highland Fire District's internal control. Accordingly, we do not express an opinion on the effectiveness of the Highland Fire District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Highland Fire District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



HintonBurdick, PLLC
Flagstaff, Arizona
October 19, 2015