

# **Cornerstone Metropolitan District No. 2**

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**Annual Financial Report**

**December 31, 2012**

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**Haynie &  
Company**

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## **Report of Independent Certified Public Accountants**

To the Board of Directors  
Cornerstone Metropolitan District No. 2

We have audited the accompanying financial statements of the governmental activities and the major funds of Cornerstone Metropolitan District No. 2 (the "District") as of and for the year ended December 31, 2012 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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 the major funds of Cornerstone Metropolitan District No. 2, as of December 31, 2012 and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Emphasis of a Matter**

As discussed in Note 12 to the financial statements, the District implemented Governmental Accounting Standards Board Statement 65, *Items Previously Reported as Assets and Liabilities*, for the year ended December 31, 2012. The District's beginning net position has been restated to reflect expensing of all debt issuance costs that had been previously capitalized. 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, as listed in the table of contents, 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 Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Cornerstone Metropolitan District No. 2's financial statements as a whole. The supplementary information section is presented for purposes of additional analysis and are not a required part of the financial statements.

The supplementary information as listed in the table of contents is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.



Littleton, Colorado  
July 15, 2013

# **Cornerstone Metropolitan District No. 2 Management's Discussion and Analysis December 31, 2012**

As management of Cornerstone Metropolitan District No. 2 (the "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 December 31, 2012.

## **Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of three components: 1) government-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. This report also contains additional supplementary information in addition to the basic financial statements and notes.

### **Government-wide financial statements**

The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The Statement of Net Position presents information on all the District's assets, deferred outflows, liabilities, and deferred inflows with the difference reported as net position.

The Statement of Activities presents information showing how the government'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 in this statement for some items that will only result in cash flows in future fiscal periods.

The governmental activities of the District relate to satisfying an intergovernmental agreement with Cornerstone Metropolitan District No. 1 and to service the District's long-term debt requirements. The government-wide financial statements can be found on pages 1 and 2 of this report.

### **Fund financial statements**

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The District currently has one fund, the Debt Service Fund.

### **Governmental funds**

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. The governmental funds provide a reconciliation to facilitate this comparison between governmental funds and governmental activities. The governmental funds financial statements are located on pages 3 and 4 of this report.

## Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The Notes to the Financial Statements can be found starting on page 6 of this report.

### Government-wide Financial Analysis

The following table shows a condensed statement of net assets as of December 31, 2012, derived from the government-wide financial statements.

#### Cornerstone Metropolitan District No. 2 Net Position

	<b>Governmental Activities 2012</b>	<b>Governmental Activities 2011 (Restated)</b>
<b>Assets:</b>		
Current assets	\$ 3,531,919	\$ 4,185,690
Other assets	-	-
<b>Total Assets</b>	<b>3,531,919</b>	<b>4,185,690</b>
<b>Liabilities &amp; Deferred Inflows:</b>		
Current liabilities & deferred inflows	869,556	841,785
Long-term and other liabilities	31,308,045	30,779,701
<b>Total Liabilities &amp; Deferred Inflows</b>	<b>32,177,601</b>	<b>31,621,486</b>
<b>Net Position:</b>		
Restricted	2,658,580	3,378,572
Unrestricted	(31,304,262)	(30,814,368)
<b>Total Net Position</b>	<b>\$ (28,645,682)</b>	<b>\$ (27,435,796)</b>

The District is the “taxing district” in a dual district structure whereby the District has and will continue to finance the construction and operation of the infrastructure for Cornerstone subdivision. The District has entered into a District Facilities Construction and Service Agreement with Cornerstone Metropolitan District No. 1. Under the agreement, District No. 1 (the “operating district”) is responsible for managing the construction of all facilities and improvements and for the operation and maintenance of all improvements not conveyed to another public entity. District No. 2 is responsible for providing the funding for all infrastructure improvements and the revenue needed to support the ongoing operation and maintenance of the improvements and public facilities. Cornerstone Metropolitan District No. 2 will ultimately pay off the “capital obligation” for construction costs as well as the “service obligation” for the excess costs of operating and maintaining the facilities.

At the end of the current fiscal year, the District has a negative unrestricted net position which is primarily a result of the issuance of the Series 2010 A and B Bonds to finance the construction of infrastructure assets owned and reported by District No 1.

The following table shows a condensed statement of activities, derived from the government-wide financial statements.

**Cornerstone Metropolitan District No. 2  
Change in Net Position**

	<b>Governmental Activities</b>	<b>Governmental Activities</b>
	<b>2012</b>	<b>2011 (Restated)</b>
	<u>                    </u>	<u>                    </u>
<b>Revenues:</b>		
Charges for services	\$ -	\$ -
Property taxes	667,734	753,075
Interest and other income	24,388	4,710
Operating grants and contributions	-	-
Capital grants and contributions	-	1,586,000
<b>Total Revenues</b>	<u>692,122</u>	<u>2,343,785</u>
<b>Expenses:</b>		
General government	17,079	19,909
Intergovernmental agreement	771,156	949,999
Interest expense	1,113,773	1,098,865
<b>Total Expenses</b>	<u>1,902,008</u>	<u>2,068,773</u>
<b>Change in Net Position</b>	(1,209,886)	275,012
<b>Net Position- Beginning</b>	<u>(27,435,796)</u>	<u>(27,710,808)</u>
<b>Net Position- Ending</b>	<u>\$ (28,645,682)</u>	<u>\$ (27,435,796)</u>

The primary reason for the decrease in net position during 2012 is the excess in debt service expenses on the 2010 B Bonds over revenues available for such debt service, as well as additions to obligations owed to District No. 1 for unfunded accrued interest on developer notes.

**Financial Analysis of the District's Funds**

As mentioned earlier, the District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Governmental funds**

The focus of the District's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the District's financing requirements. In particular, unrestricted fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

Debt Service Fund revenues were \$653,672 in 2012 and consisted primarily of property and specific ownership tax.

Debt Service Fund expenditures totaled \$1,373,664 in 2012 and were primarily related to interest and letter of credit fees on the 2010A and B Bonds as well as funding provided to District No. 1 used towards community operations.

As of the end of 2012, the District's governmental fund reported an ending fund balance of \$2,658,580. This balance is restricted for future debt service.

### **Budget variances**

District revenues were less than budget due to non-payment of property taxes by some owners and the development fees that were budgeted being collected in 2011 rather than 2012. Expenditures were favorable to budget do to the low variable interest rate paid on the 2010 B Bonds. The Debt Service Fund budget to actual report can be found in the Supplementary Information section of this report, on page 20.

### **Long-term debt**

As of December 31, 2012 the Series 2010 A and B Bonds principal balance remained at \$22,200,000 as no principal payments were due during 2012. Details regarding the District's long-term debt are located in Note 5 starting on page 12 of this report.

### **Economic Conditions and Outlook:**

The County Assessor reassessed the value of the property in the District effective January 1, 2012 which were used to set 2011 property taxes payable in 2012. The valuations reflected a reduction in the District's assessed value of 32%. For the 2012 budget the District increased the mill levy rate from 39 mills to 52 mills to offset the reduction in assessed values. However, further declines are expected which will cause funding shortfalls for both the 2010 Bonds and to District No. 1 for operations as the District is currently only able to increase the total mill levy to a maximum of 55 mills.

The District is dependent on the timely payment of property taxes by the District constituents and due to delinquencies on payment by the Developer and Club, was required to draw on the Reserve Fund on December 1, 2012 to fund the shortfall in the interest payment due on the Series 2010A Bonds. The District subsequently replenished the Reserve Fund back to a balance of \$520,000 in January 2013 but was forced to draw on the reserve fund again to make the June 1, 2013 bond interest payment. See Note 5 on page 13 for additional information.

### **Request for Information**

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. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Cornerstone Metropolitan District No. 2, c/o Robertson & Marchetti, P.C., 28 Second Street, Suite 213, Edwards, CO 81632, (970) 926-6060.

## **Basic Financial Statements**

**Cornerstone Metropolitan District No. 2**  
**Statement of Net Position**  
**December 31, 2012**

<b>Assets</b>	<b>Governmental Activities</b>
Cash - unrestricted	\$ 494
Cash - restricted	2,818,930
Due from treasurer	4,132
Property tax receivable	708,363
Total assets	<u>3,531,919</u>
<b>Liabilities</b>	
Intergovernmental payable	25,621
Accrued expenses	160,005
Accrued interest payable	38,048
Non-current capital and service obligations due to Cornerstone Metro Dist. No. 1	9,108,045
Bonds payable	22,200,000
Total liabilities	<u>31,531,719</u>
<b>Deferred Inflows of Resources</b>	
Deferred property tax revenue	645,882
Total deferred inflows of resources	<u>645,882</u>
<b>Net Position</b>	
Restricted for debt service	2,658,580
Unrestricted	<u>(31,304,262)</u>
Total Net Position	<u>(28,645,682)</u>
Total Liabilities, Deferred Inflows and Net Position	<u>\$ 3,531,919</u>

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

**Cornerstone Metropolitan District No. 2**  
**Statement of Activities**  
**For the Year Ended December 31, 2012**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government
					Governmental Activities
Primary government:					
Governmental activities:					
General government	\$ 17,079	\$ -	\$ -	\$ -	\$ (17,079)
Intergovernmental agreement	771,156	-	-	-	(771,156)
Interest and related costs on long term debt	1,113,773	-	-	-	(1,113,773)
	<u>1,902,008</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,902,008)</u>
General revenues:					
Property taxes					620,917
Specific ownership taxes					46,817
Investment income					24,388
Total general revenues and transfers					<u>692,122</u>
Change in net position					(1,209,886)
Net position - beginning of year (as restated)					<u>(27,435,796)</u>
Net position - end of year					<u>\$ (28,645,682)</u>

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

**Cornerstone Metropolitan District No. 2**  
**Governmental Funds Balance Sheet**  
**and Reconciliation of Fund Balances to Net Position**  
**December 31, 2012**

	<b>Debt Service Fund</b>
<b>Assets</b>	
Cash - unrestricted	\$ 494
Cash - restricted	2,818,930
Due from treasurer	4,132
Property taxes receivable	708,363
Total assets	\$ 3,531,919
<b>Liabilities</b>	
Intergovernmental payable	\$ 1,590
Accrued expenses	163,386
Total liabilities	164,976
<b>Deferred Inflows of Resources</b>	
Deferred property tax revenue	708,363
Total deferred inflows of resources	708,363
<b>Fund Balances</b>	
Restricted for debt service	2,658,580
Total Fund Balances	2,658,580
<b>Total Liabilities, Deferred Inflows, and Fund Balance</b>	<b>\$ 3,531,919</b>
Total governmental fund balance per above	\$ 2,658,580
<p>Amounts reported for governmental activities in the statement of net position are excluded from the governmental fund balance because:</p> <p>Long term assets or liabilities not receivable or payable in the current year are excluded in the governmental funds. Interest on long-term debt is recognized as an expenditure in governmental funds when due. These items consist of:</p>	
Capital and service obligations due to Cornerstone Metro Dist. No. 1	(9,108,045)
Bonds payable	(22,200,000)
Prior year taxes not yet received	38,450
Accrued interest payable	(34,667)
Net position of governmental activities	\$ (28,645,682)

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

**Cornerstone Metropolitan District No. 2**  
**Governmental Fund Revenues, Expenditures,**  
**and Changes in Fund Balances**  
**For the Year Ended December 31, 2012**

	<b>Debt Service</b>
<b>Revenues:</b>	
Property taxes	\$ 582,467
Specific ownership taxes	46,817
Investment income	24,388
Total General Revenues	653,672
<b>Expenses:</b>	
General government	
Operations transfer to	
Cornerstone Metro Dist. No. 1	242,812
Treasurer's fees	6,569
Debt service	
Letter of credit fees	612,077
Treasurer's fees	10,510
Remarketing fees	34,000
Bond interest	458,156
Wire, trustee and rating agency fees	9,540
Total Expenditures	1,373,664
Excess (Deficiency) of Revenues over expenditures	(719,992)
Net change in fund balance	(719,992)
Fund balances:	
Beginning of the year	3,378,572
End of the year	\$ 2,658,580

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

**Cornerstone Metropolitan District No. 2**  
**Reconciliation of the Statement of Revenues, Expenditures**  
**and Changes in Fund Balances of Governmental Funds**  
**to the Statement of Activities**  
**For the Year Ended December 31, 2012**

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

Net change in fund balance—total governmental funds	\$ (719,992)
<p>Property taxes levied but uncollected, net of the amount of such taxes owed to District No. 1, are reported in the Statement of Activities as income but do not provide current financial resources and, therefore, are not reported in the funds.</p>	
Uncollected property taxes	62,481
Less amount owed to District No. 1	(24,031)
<p>Capital and service obligations reported in the Statement of Activities do not provide or consume current financial resources and, therefore, are not reported as revenues or expenditures in governmental funds.</p>	
	<u>(528,344)</u>
Change in net position of governmental activities	<u>\$ (1,209,886)</u>

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

# **Cornerstone Metropolitan District No. 2**

## **Notes to Financial Statements**

### **December 31, 2012**

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#### **1. Definition of Reporting Entity**

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Cornerstone Metropolitan District No. 2 (the District), a quasi-municipal corporation and political subdivision of the State of Colorado, was organized concurrently with Cornerstone Metropolitan District No. 1 (collectively the Districts) by District Court Order on November 15, 2004, as amended December 22, 2004, and is governed pursuant to provisions of the Colorado Special District Act (Title 32). The Districts' service area is located in both Montrose County and in Ouray County. The Districts operate under a Consolidated Service Plan to provide financing for the design, acquisition, construction and installation of essential public purpose facilities including streets, water, storm drainage, sanitary sewer, parks and recreation, transportation, television relay, mosquito control and fire protection, and the operation and maintenance of the Districts. Under the Service Plan, the District is intended to be the Taxing District related to Cornerstone Metropolitan District No. 1, the Operating District.

The District follows the Governmental Accounting Standards Board (GASB) accounting pronouncements which provide guidance for determining which governmental activities, organizations and functions should be included within the financial reporting entity. GASB pronouncements set forth the financial accountability of a governmental organization's elected governing body as the basic criterion for including a possible component governmental organization in a primary government's legal entity. Financial accountability includes, but is not limited to, appointment of a voting majority of the organization's governing body, ability to impose its will on the organization, a potential for the organization to provide specific financial benefits or burdens and fiscal dependency.

The District has no employees and contracts for all of its management and professional services.

The District is not financially accountable for any other organization, nor is the District a component unit of any other primary governmental entity.

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#### **2. Summary of Significant Accounting Policies**

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The more significant accounting policies of the District are described as follows:

##### **Government-wide and Fund Financial Statements**

The government-wide financial statements include the statement of net position and the statement of activities. These financial statements include all of the activities of the District.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**2. Summary of Significant Accounting Policies (continued)**

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Governmental activities are normally supported by property taxes collected. Both statements distinguish between governmental activities, which normally are supported by taxes and business-type activities, which rely to a significant extent on fees and charges for support.

The statement of net position reports all financial and capital resources of the District. The difference between the assets, deferred outflows, liabilities, and deferred inflows of the District is reported as net position. Since District No. 1 is ultimately responsible for owning and operating the infrastructure of the community, and District No. 2 is ultimately responsible to provide funding for such, the net position of the District show a negative balance as District No. 1 reports the capital assets financed in part by District No. 2.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. 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. Taxes and other items not properly included among program revenues are reported instead as general revenues.

**Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

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. Expenditures for redemption of bonds are recorded as a reduction in liabilities.

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. The major sources of revenue susceptible to accrual are property taxes. All other revenue items are considered to be measurable and available only when cash is received by the District. Expenditures, other than interest on long-term obligations, are recorded when the liability is incurred or the long-term obligation paid.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**2. Summary of Significant Accounting Policies (continued)**

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The District reports the following major governmental funds:

The Debt Service Fund accounts for the resources accumulated and payments made for principal and interest on long-term debt and contractual obligations to District No. 1.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes received from other governmental activities.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

**Budgets**

In accordance with the State Budget Law, the District's Board of Directors holds public hearings in the fall each year to approve the budget and appropriate the funds for the ensuing year. The appropriation is at the total fund expenditures level and lapses at year end. The District's Board of Directors can modify the budget by line item within the total appropriation without notification. The appropriation can only be modified upon completion of notification and publication requirements. The budget includes each fund presented on the modified accrual basis of accounting.

**Fund Equity**

Fund balance for governmental funds should be reported in classifications that comprise a hierarchy based on the extent to which the government is bound to honor constraints on the specific purposes for which spending can occur. Governmental funds report up to five classifications of fund balance: nonspendable, restricted, committed, assigned, and unassigned. Because circumstances differ among governments, not every government or every governmental fund will present all of these components. The following classifications describe the relative strength of the spending constraints:

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**2. Summary of Significant Accounting Policies (continued)**

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- *Nonspendable fund balance* - The portion of fund balance that cannot be spent because it is either not in spendable form (such as prepaid amounts or inventory) or legally or contractually required to be maintained intact.
- *Restricted fund balance* - The portion of fund balance that is constrained to being used for a specific purpose by external parties (such as bondholders), constitutional provisions, or enabling legislation.
- *Committed fund balance* - The position of fund balance that can only be used for specific purposes pursuant to constraints imposed by formal action of the government's highest level of decision-making authority, the Board of Directors. The constraint may be removed or changed only through formal action of the Board of Directors.
- *Assigned fund balance* - The position of fund balance that is constrained by the government's intent to be used for specific purposes, but is neither restricted nor committed. Intent is expressed by the Board of Directors to be used for a specific purpose. Constraints imposed on the use of assigned amounts are more easily removed or modified than those imposed on amounts that are classified as committed.
- *Unassigned fund balance* - The residual portion of fund balance that does not meet any of the criteria described above. If more than one classification of fund balance is available for use when an expenditure is incurred, it is the District's policy to use the most restrictive classification first.

**Fund Balance Classifications**

The total fund balance of the governmental funds was \$2,658,580 as of December 31, 2012. The entire balance was restricted for the payment of future debt service principal, interest and related costs, as well as operational funding to District No. 1.

**New Accounting Pronouncements**

Effective January 1, 2012, the District implemented the provisions of GASB No. 63, "Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position" (GASB No. 63).

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**2. Summary of Significant Accounting Policies (continued)**

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GASB No. 63 provides guidance for reporting deferred outflows and deferred inflows of resources as introduced and defined in GASB Concepts Statement No. 4 “Elements of Financial Statements” (Concepts Statement No. 4). Concepts Statement No. 4 defines a deferred outflow of resources as a consumption of net assets that is applicable to a future reporting period. A deferred inflow of resources is defined as an acquisition of net assets applicable to a future reporting period. The impact on the District’s financial statements has been to replace the term “net assets” with “net position”.

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**3. Cash and Investments**

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The Colorado Public Deposit Protection Act (PDPA) requires that all units of local government deposit cash in eligible public depositories. Eligibility is determined by state regulators. Amounts on deposit in excess of federal insurance levels must be collateralized. The eligible collateral is determined by the PDPA. PDPA allows the institution to create a single collateral pool for all public funds.

The pool for all the uninsured public deposits as a group is to be maintained by another institution or held in trust. The market value of the collateral must be at least equal to 102% of the aggregate uninsured deposits.

The State Commissioners for banks and financial services are required by statute to monitor the naming of eligible depositories and reporting of the uninsured deposits and assets maintained in the collateral pools.

The majority of the funds on hand in the Debt Service Fund are assigned for future debt service.

As of December 31, 2012, the District’s cash deposits had a bank balance of \$0 and a carrying balance of \$0.

**Investments**

The District has not adopted a formal investment policy, however, the District follows state statutes regarding investments.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**3. Cash and Investments (continued)**

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The District generally limits its concentration of investments to those noted with an asterisk (\*) below, which are believed to have minimal credit risk, minimal interest rate risk and no foreign currency risk. Additionally, the District is not subject to concentration risk disclosure requirements or subject to investment custodial credit risk for investments that are in the possession of another party.

Colorado revised statutes limit investment maturities to five years or less unless formally approved by the Board of Directors. Such actions are generally associated with a debt service reserve or sinking fund requirements.

Colorado statutes specify investment instruments meeting defined rating and risk criteria in which local governments may invest which include:

- Obligations of the United States, certain U.S. government agency securities and the World Bank
- General obligation and revenue bonds of U.S. local government entities
- Bankers acceptances of certain banks
- Commercial paper
- Written repurchase agreements and certain reverse repurchase agreements collateralized by certain authorized securities
- Guaranteed investment contracts
- \* Local government investment pools

The local government investment pools, which include the Colorado Surplus Asset Fund Trust (CSAFE) and the Colorado Local Government Liquid Asset Trust (Colotrust) are both rated AAAM by Standard & Poor's.

As of December 31, 2012, the District had the following investments:

<b>Investment</b>	<b>Maturity</b>	<b><u>Fair Value</u></b>
Colorado Surplus Asset Trust Fund (CSAFE)	Weighted average under 60 days	<u>\$ 2,819,424</u>

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**3. Cash and Investments (continued)**

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**CSAFE**

During 2012, the District invested in the Colorado Surplus Asset Fund Trust (CSAFE), which is an investment vehicle established by State statutes for local government entities to pool surplus funds. The State Securities Commission administers and enforces all State statutes governing the Trust. The Trust is similar to a money market fund with each share valued at \$1.00. CSAFE may invest in U.S. Treasury securities and repurchase agreements collateralized by U.S. Treasury securities. A designated custodial bank serves as custodian for CSAFE's investment portfolio and services as the depository in connection with direct investments and withdrawals. The custodian's internal records segregate investments owned by CSAFE. As of December 31, 2012, the District had \$2,819,424 invested in CSAFE.

Cash and investments as of December 31, 2012 are classified in the accompanying financial statements as follows:

	<u>2012</u>
Cash - Unrestricted	\$ 494
Cash - Restricted	<u>2,818,930</u>
	<u>\$ 2,819,424</u>

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**4. Long-Term Capital and Service Obligations Receivable**

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Cornerstone Metropolitan District No. 2 is obligated under the Master Intergovernmental agreement between the Districts to provide funding for all public infrastructure improvements (capital obligation) to provide the revenue needed to support the ongoing operation and maintenance of the improvements and public facilities (service obligation). These items represent the portion of the obligations not yet reimbursed by Cornerstone Metropolitan District No. 1 as of December 31, 2012.

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**5. Long-Term Liabilities**

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On December 15, 2010, the District concurrently issued \$5,200,000 in Series 2010A Limited Tax General Obligation Refunding Bonds and \$17,000,000 in Series 2010B Subordinate Variable Rate Limited Tax General Obligation Refunding Bonds. The net proceeds of the bonds were transferred to Cornerstone Metropolitan District No. 1 and used to pay off the Series 2006 Bonds previously issued by Cornerstone Metropolitan District No. 1.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**5. Long-Term Liabilities (continued)**

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The following is an analysis of changes in the District's long-term debt for the year ended December 31, 2012:

	<b>Balance December 31, 2011</b>	<b>Additions</b>	<b>Payments</b>	<b>Balance December 31, 2012</b>	<b>Due Within One Year</b>
Series 2010A Bonds	\$ 5,200,000	\$ -	\$ -	\$ 5,200,000	\$ -
Series 2010B Bonds	<u>17,000,000</u>	<u>-</u>	<u>-</u>	<u>17,000,000</u>	<u>-</u>
	<u>\$ 22,200,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 22,200,000</u>	<u>\$ -</u>

The detail of the District's long-term debt outstanding at December 31, 2012 is as follows:

**Series 2010A**

The Series 2010A Bonds bear interest at a fixed rate of 8.0% with interest payments due semi-annually on June 1 and December 1 of each year. Principal payments are due on December 1 of each year beginning in 2015, continuing through final maturity in 2040. The Bonds are subject to redemption prior to maturity at the option of the District on or after December 1, 2021, without premium. The bonds are payable from the net pledged revenues, including ad valorem property taxes, specific ownership taxes, development fees and other legally available revenues. The property tax mill levy used to pay the bonds is required to be no less than 25 mills and not greater than 40 mills. The Bonds are also secured by a reserve fund in the amount of \$520,000, which was drawn on in the amount of \$25,583 in 2012 to fund the shortfall in the Series 2010A interest payment and was replenished by the District in January of 2013. See Note 11 for additional information.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**5. Long-Term Liabilities (continued)**

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Below is a summary of the future maturities of the Series 2010A Bonds:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ -	\$ 416,000	\$ 416,000
2014	-	416,000	416,000
2015	5,000	416,000	421,000
2016	10,000	415,600	425,600
2017	5,000	414,800	419,800
2018-2022	145,000	2,054,800	2,199,800
2023-2027	430,000	1,955,200	2,385,200
2028-2032	845,000	1,722,000	2,567,000
2033-2037	1,455,000	1,294,000	2,749,000
2038-2040	<u>2,305,000</u>	<u>456,800</u>	<u>2,761,800</u>
Total	<u>\$ 5,200,000</u>	<u>\$ 9,561,200</u>	<u>\$ 14,761,200</u>

**Series 2010B**

The Series 2010B Bonds bear interest at a variable rate which is currently reset on a weekly basis by the remarketing agent. Interest for the previous month is payable on the first business day of the following month. Principal payments are due on December 1 of each year beginning in 2023 and continuing through the final maturity date in 2046. The Bonds are subject to redemption prior to maturity at the option of the District at any time, without premium. The Bonds are subordinate to the Series 2010A Bonds and are payable from the remaining net pledged revenues, including ad valorem property taxes, specific ownership taxes and development fees. In the event that a mill levy of 25 mills (the minimum levy required by the 2010A Bonds), along with other available revenues, is insufficient to pay the debt service on the bonds, the total mill levy will be increased up to a maximum of 30 mills. The Series 2010B Bonds are also secured by an irrevocable direct pay letter of credit issued by the Bank of America, N.A. The letter of credit is available only to be used towards the Series 2010B Bonds, not the Series 2010A Bonds. The initial term of the letter of credit expired on December 1, 2011 but automatically extended and will continue to automatically extend annually unless terminated by the bank. The letter of credit fees are paid on a quarterly basis at a current annual rate of 3.50%. The letter of credit is secured by a reimbursement agreement with the original developer, Cornerstone Montrose, LLC and Hunt Realty Investments, Inc. which are jointly responsible for any draws and reimbursements on the letter of credit.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**5. Long-Term Liabilities (continued)**

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Annual interest payments will be calculated based on a variable rate and continue to be paid until the remaining principal is paid in full. The Subordinate Series 2010B Bonds are also subject to a mandatory sinking fund redemption, in part, by lot, on December 1, 2023 and on each December 1 thereafter prior to the maturity date. Future estimated principal and interest payments are as follows, based on an estimated historical average interest rate of approximately 2.02%:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ -	\$ 343,400	\$ 343,400
2014	-	343,400	343,400
2015	-	343,400	343,400
2016	-	343,400	343,400
2017	-	343,400	343,400
2018-2022	-	1,717,000	1,717,000
2023-2027	1,225,000	1,670,540	2,895,540
2028-2032	1,660,000	1,529,948	3,189,948
2033-2037	2,170,000	1,342,391	3,512,391
2038-2042	4,520,000	1,082,215	5,602,215
2043-2046	<u>7,425,000</u>	<u>389,355</u>	<u>7,814,355</u>
Total	<u>\$ 17,000,000</u>	<u>\$ 9,448,449</u>	<u>\$ 26,448,449</u>

**Debt Authorization**

On November 2, 2004, the District's electors authorized the issuance of indebtedness totaling \$787,500,000 at an interest rate not to exceed 12%. The following schedule shows the amounts authorized and issued as of December 31, 2012:

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**5. Long-Term Liabilities (continued)**

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	<b>Authorized November 2, 2004</b>	<b>Authorization Used, Series 2010</b>	<b>Remaining at December 31, 2012</b>
Streets	\$ 60,000,000	\$ -	\$ 60,000,000
Traffic & safety	60,000,000	-	60,000,000
Water	60,000,000	-	60,000,000
Sanitary sewer and storm drainage	60,000,000	-	60,000,000
Parks and recreation	60,000,000	-	60,000,000
Transportation	60,000,000	-	60,000,000
Television relay	60,000,000	-	60,000,000
Mosquito control	60,000,000	-	60,000,000
Fire and ambulance	60,000,000	-	60,000,000
Operations and maintenance	60,000,000	-	60,000,000
Intergovernmental contracts	60,000,000	-	60,000,000
Reimbursement agreements	60,000,000	-	60,000,000
Management services	7,500,000	-	7,500,000
Refunding of debt	<u>60,000,000</u>	<u>22,200,000</u>	<u>37,800,000</u>
Total	<u>\$ 787,500,000</u>	<u>\$ 22,200,000</u>	<u>\$ 765,300,000</u>

However, pursuant to the Service Plan, the District will not issue more than \$30,000,000 in indebtedness.

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**6. Net Position**

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Restricted assets include net position that are restricted for use either externally imposed by grantors, contributors or laws and regulations of other governments or imposed by law through constitutional provisions or enabling legislation.

The District's unrestricted net position as of December 31, 2012 totaled \$(31,342,712), because the infrastructure paid for by the debt of the District is owned and reported by District No. 1.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**7. Related Parties**

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The original Developer of the property which constitutes the District is Cornerstone Montrose LLC, a Delaware limited liability company, and a wholly-owned subsidiary of Hunt Realty Investments, Inc. (f.k.a. Hunt Realty Corp.). Some of the members of the Board of Directors were officers, employees or associated with the Developer and may have conflicts of interest in dealing with the District.

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**8. Economic Dependencies**

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The District is dependent on the property taxes paid by District constituents, the majority of which are paid by the Developer and related club entity. The District is owed \$62,481 for taxes levied but which remain outstanding as of December 31, 2012.

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**9. Risk Management**

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The District is exposed to various risks of loss related to torts, thefts of, damage to, or destruction of assets; errors or omissions; injuries to employees, or acts of God.

The District is a member of the Colorado Special Districts Property and Liability Pool (Pool). The Pool is an organization created by intergovernmental agreement to provide property, liability, public officials' liability, boiler and machinery and workers compensation coverage to its members. Settled claims have not exceeded this coverage in any of the past three fiscal years.

The District pays annual premiums to the Pool for liability, property and public officials' liability coverage. In the event aggregated losses incurred by the Pool exceed amounts recoverable from reinsurance contracts and funds accumulated by the Pool, the Pool may require additional contributions from the Pool members. Any excess funds which the Pool determines are not needed for purposes of the Pool may be returned to the members pursuant to a distribution formula.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**10. Intergovernmental Agreements**

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**District Facilities Construction and Service Agreement**

On December 16, 2004, the Districts entered into a Districts Facilities Construction and Service Agreement (the Master IGA). The Master IGA provides that the District is to finance the construction, maintenance and operations of the facilities constructed and operated by Cornerstone Metropolitan District No.1 as provided by the Consolidated Service Plan. The District is to finance such activities from their annual certification of a mill levy, specific ownership taxes and development fees. The mill levy is limited by the Service Plan wherein the combined maximum mill levy shall not exceed 55.000 mills, with the maximum operations mill levy not to exceed 20.000 mills, and the maximum debt mill levy not to exceed 40.000 mills.

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**11. Tax, Spending and Debt Limitations**

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Article X, Section 20 of the Colorado Constitution, commonly known as the Taxpayer's Bill of Rights (TABOR) contains tax, spending, revenue and debt limitations which apply to the State of Colorado and all local governments.

Spending and revenue limits are determined based on the prior year's Fiscal Year Spending adjusted for allowable increases based upon inflation and local growth. Fiscal Year Spending is generally defined as expenditures plus reserve increases with certain exceptions. Revenue in excess of the Fiscal Year Spending limit must be refunded unless the voters approve retention of such revenue.

TABOR requires local governments to establish Emergency Reserves. These reserves must be at least 3% of Fiscal Year Spending (excluding bonded debt service). At December 31, 2012, the District was not required to have an emergency reserve as all operations are performed by District No. 1.

On November 2, 2004, the District's voters authorized the District to increase property taxes \$60,000,000 annually, without limitation to rate, to pay the District's operations, maintenance and other expenses. The election also allows the District to collect, spend and retain all revenues without regard to the limitations contained within Article X, Section 20 of the Colorado constitution.

The District's management believes it is in compliance with the provisions of TABOR. However, TABOR is complex and subject to interpretation. Many of the provisions, including the interpretation of how to calculate Fiscal Year Spending limits will require judicial interpretation.

**Cornerstone Metropolitan District No. 2**  
**Notes to Financial Statements (continued)**  
**December 31, 2012**

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**12. Implementation of GASB Statement No. 65**

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The District implemented Government Accounting Standards Board Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which requires debt issuance costs, previously reported as an asset and amortized, to be recognized as an outflow at the time such costs are incurred. As such, the financial statements report a restatement of the beginning net position in the amount of \$480,922, which was the unamortized debt issuance cost at December 31, 2011.

## **Supplementary Information**

**Cornerstone Metropolitan District No. 2**  
**Statement of Revenue, Expenditures**  
**and Changes in Fund Balance—Actual and Budget**  
**Governmental Fund Type—Debt Service Fund**  
**For the Year Ended December 31, 2012**

	<b>Original and Final Budget</b>	<b>Actual</b>	<b>Variance Favorable (Unfavorable)</b>
<b>Revenue:</b>			
Property taxes	\$ 644,948	\$ 582,467	\$ (62,481)
Specific ownership taxes	56,387	46,817	(9,570)
Investment income	2,797	24,388	21,591
Development fees	182,000	-	(182,000)
Total Revenue	886,132	653,672	(232,460)
<b>Expenditures:</b>			
General government			
Operations transfer to			
Cornerstone Metro Dist. No. 1	262,816	242,812	20,004
Treasurer's fees	6,928	6,569	359
Contingency	1,000	-	1,000
Debt service			
Letter of credit fees	611,858	612,077	(219)
Treasurer's fees	11,084	10,510	574
Remarketing fees	34,000	34,000	-
Bond interest	586,000	458,156	127,844
Wire, trustee and rating agency fees	9,040	9,540	(500)
Contingency	182,000	-	182,000
Total Expenditures	1,704,726	1,373,664	331,062
<b>Excess Revenue Over (Under)</b>			
<b>Expenditures</b>	(818,594)	(719,992)	98,602
<b>Change in fund balance</b>	(818,594)	(719,992)	98,602
<b>Fund Balance—Beginning of year</b>	1,797,760	3,378,572	1,580,812
<b>Fund Balance—End of Year</b>	\$ 979,166	\$ 2,658,580	\$ 1,679,414