

Cornerstone Metropolitan District No. 2

Annual Financial Report

December 31, 2010

Table of Contents

	Page
INDEPENDENT AUDITOR’S REPORT	I
Management Discussion and Analysis	II
BASIC FINANCIAL STATEMENTS	
Government-wide Financial Statements:	
Statement of Net Assets	1
Statement of Activities	2
Governmental Funds Balance Sheet and Reconciliation of Fund Balances to Net Assets	3
Governmental Fund Revenues, Expenditures, and Changes in Fund Balances	4
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities	5
Notes to Basic Financial Statements	6-17
SUPPLEMENTARY INFORMATION	
Statement of Revenue, Expenditures and Changes in Fund Balance —Actual and Budget—Governmental Fund Type—Debt Service Fund.....	18



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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 as of and for the year ended December 31, 2010, which collectively comprise the District's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion 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 in accordance with the Colorado Local Government Audit Law. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

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, 2010, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis in Section II and Statements of Revenue, Expenditures, and Changes in Fund Balance – Actual and Budget for Debt Service is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the District's basic financial statements taken as a whole. The accompanying supplemental information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the District's basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the District's basic financial statements taken as a whole.

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Littleton, Colorado
June 29, 2011



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Cornerstone Metropolitan District No. 2 Management's Discussion and Analysis December 31, 2010

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, 2010.

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 Assets presents information on all the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets 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 government's net assets changed during the most recent fiscal year. All changes in net assets 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.

For 2010, 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 only 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, 2010, derived from the government-wide financial statements.

Cornerstone Metropolitan District No. 2	
Net Assets	
	Governmental Activities
	<u>2010</u>
Assets:	
Current assets	\$ 3,253,432
Other assets	496,105
Total Assets	<u><u>3,749,537</u></u>
Liabilities:	
Current liabilities	871,113
Long-term and other liabilities	30,093,127
Total Liabilities	<u><u>30,964,240</u></u>
Net Assets:	
Unrestricted	<u>(27,214,703)</u>
Total Net Assets	<u><u>\$ (27,214,703)</u></u>

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 the Cornerstone development. 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. The District 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 negative unrestricted net assets which is the result of the District having the liabilities for the cost of the infrastructure but no capital assets, since these are owned by District No. 1. The District’s revenues consisted primarily of property tax and specific ownership tax revenues.

The changes in net assets for the year ended December 31, 2010:

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

	Governmental Activities 2010
Revenues:	
Property taxes	\$ 763,609
Interest and other income	1,156
Operating grants and contributions	15,779
Capital grants and contributions	217,383
Total Revenues	997,927
Expenses:	
General government	20,119
Intergovernmental agreement	1,673,347
Interest expense	51,418
Total Expenses	1,744,884
Change in Net Assets	(746,957)
Net Assets- Beginning	(26,467,746)
Net Assets- Ending	\$ (27,214,703)

The primary reason for the decrease in net assets during 2010 is the increase in the service obligation owed to District No. 1 due to the shortfall in currently available funding from the District.

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.

Debt Service Fund revenues were \$764,765 in 2010 and consisted mostly of property and specific ownership tax revenues. The District also issued \$22,200,000 in bonds, the net proceeds of which were transferred to District No. 1 to pay off the District No. 1 bonds.

Debt Service Fund expenditures were \$1,292,009 in 2010, primarily operating and capital transfers to Cornerstone Metropolitan District No. 1 as part of the District Facilities Construction and Service Agreement, as well as the costs related to the issuance and debt service costs associated with the bond issuance.

As of the end of 2010, the District's governmental fund reported an ending fund balance of \$2,402,548. These balances are broken down into categories of assigned for debt service and unassigned.

Budget variances

The District amended the budget one time during 2010 to account for the issuance of the bonds. The Debt Service Fund ending fund balance finished the year \$16,840 behind budget, which is primarily attributable to

debt service costs being greater than anticipated. The Debt Service Fund budget to actual report can be found in the Supplementary Information section of this report, on page 18.

Long-term debt

The District increased debt by \$22,200,000, the proceeds of which were used to pay off Cornerstone Metropolitan District No. 1 Series 2006 Bonds. Details regarding the District's long-term debt are located in Note 5 on pages 12-15 of this report.

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 Assets
December 31, 2010

Assets	Governmental Activities
Investments in pooled cash - unrestricted	\$ 109,246
Investments in pooled cash - restricted	2,433,384
Due from treasurer	2,228
Property tax receivable	708,574
Bond issue costs, net of amortization	<u>496,105</u>
Total assets	<u>3,749,537</u>
Liabilities	
Accounts payable	55,780
Intergovernmental payable	51,393
Due to treasurer	3,948
Accrued expenses	31,189
Deferred property tax revenue	708,574
Accrued interest payable	20,229
Non-current service obligation due to Cornerstone Metro Dist. No. 1	4,386,106
Non-current capital obligation due to Cornerstone Metro Dist. No. 1	3,507,021
Bonds payable	<u>22,200,000</u>
Total liabilities	<u>30,964,240</u>
Net Assets	
Unrestricted	<u>(27,214,703)</u>
Total Net Assets	<u>(27,214,703)</u>
Total Liabilities and Net Assets	<u>\$ 3,749,537</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, 2010

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>			<u>Net (Expense) Revenue and Changes in Net Assets</u>
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	<u>Primary Government</u>
					<u>Governmental Activities</u>
Primary government:					
Governmental activities:					
General government	\$ 20,119	\$ -	\$ -	\$ -	\$ (20,119)
Intergovernmental agreement	1,673,347	-	15,779	-	(1,657,568)
Interest and related costs on long term debt	51,418	-	-	217,383	165,965
	1,744,884	-	15,779	217,383	(1,511,722)
General revenues:					
Property taxes					715,535
Specific ownership taxes					48,074
Investment income					1,156
Total general revenues and transfers					764,765
Change in net assets					(746,957)
Net assets - beginning of year					(26,467,746)
Net assets - end of year					\$ (27,214,703)

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 Assets
December 31, 2010

Assets	Debt Service Fund
Investments in pooled cash - unrestricted	\$ 109,246
Investments in pooled cash - restricted	2,433,384
Due from treasurer	2,228
Property taxes receivable	708,574
Total assets	<u>\$ 3,253,432</u>
Liabilities	
Accounts payable	\$ 55,780
Intergovernmental payable	51,393
Due to treasurer	3,948
Accrued expenses	31,189
Deferred property tax revenue	708,574
Total liabilities	<u>850,884</u>
Fund Balances	
Assigned for debt service	2,402,195
Unassigned	353
Total Fund Balances	<u>2,402,548</u>
Total Liabilities and Fund Balance	<u>\$ 3,253,432</u>
Total governmental fund balance per above	\$ 2,402,548
Amounts reported for governmental activities in the statement of net assets excluded from the governmental fund balance because:	
Other long-term assets are not available to pay for current period expenditures, and therefore, are not reported in the funds.	
Bond issue costs, net of amortization	496,105
Long term liabilities not payable in the current year are excluded as liabilities in the governmental funds. Interest on long-term debt is recognized as an expenditure in governmental funds when due. These liabilities consist of:	
Capital and service obligations due to Cornerstone Metro Dist. No. 1	(7,893,127)
Bonds payable	(22,200,000)
Accrued interest payable	(20,229)
Net assets of governmental activities	<u>\$ (27,214,703)</u>

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, 2010

	Debt Service
Revenues:	
Property taxes	\$ 715,535
Specific ownership taxes	48,074
Investment income	1,156
Total General Revenues	764,765
Expenses:	
General government	
Operations transfer to	
Cornerstone Metro Dist. No. 1	267,291
Capital transfer to	
Cornerstone Metro Dist. No. 1	477,305
Treasurer's fees	20,119
Debt service	
Letter of credit fees	28,421
Bond interest	2,768
Bond issuance costs, net of amortization	496,105
Total Expenditures	1,292,009
Excess (Deficiency) of Revenues over expenditures	(527,244)
Other financing sources/uses:	
Bond proceeds	22,200,000
Intergovernmental transfer to	
Cornerstone Metro Dist. No. 1	(19,503,673)
Development fees	217,383
Intergovernmental contribution	15,779
Total othe financing sources/uses	2,929,489
Net change in fund balance	2,402,245
Fund balances:	
Beginning of the year	303
End of the year	\$ 2,402,548

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, 2010

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

Net change in fund balance—total governmental funds	\$ 2,402,245
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Long-term debt 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. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.

Bond proceeds	(22,200,000)
Bond issuance costs	496,105
Accrued interest expense	(20,229)

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.

	<u>18,574,922</u>
Change in net assets of governmental activities	<u>\$ (746,957)</u>

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

Cornerstone Metropolitan District No. 2

Notes to Financial Statements

December 31, 2010

1. Definition of Reporting Entity

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.

2. Summary of Significant Accounting Policies

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 assets and the statement of activities. These financial statements include all of the activities of the District. For the most part, the effect of interfund activity has been removed from these statements.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

2. Summary of Significant Accounting Policies (continued)

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 assets reports all financial and capital resources of the District. The difference between the assets and liabilities of the District is reported as net assets. 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 assets 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, 2010

2. Summary of Significant Accounting Policies (continued)

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. During the year ended December 31, 2010, supplementary appropriations approved by the District modified the appropriations in the Debt Service Fund to account for the issuance of bonds.

Bond Issue Costs

In the government-wide financial statements, bond issuance costs are reported as deferred charges and amortized over the term of related debt.

In the fund financial statements, governmental fund types recognize bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources.

Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

2. Summary of Significant Accounting Policies (continued)

Fund Equity

In the fund financial statements, governmental funds report restrictions of fund balance for amounts that are legally segregated or are not subject to future appropriation. Assignments of fund balances indicate the Board of Director's intention for future utilization of such funds and are subject to change by management.

The District considers all unassigned fund balances to be "reserves" for future operations or capital replacement as defined within Article X, Section 20 of the Constitution of the State of Colorado (see Note 10).

Fund Balance Classifications

The total fund balance of the governmental funds was \$2,402,548 as of December 31, 2010. Of this balance, \$2,402,195 was assigned for the payment of future debt service principal, interest and related costs and the remaining \$353 is unassigned.

3. Cash and Investments

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.

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

As of December 31, 2010, the District's cash deposits had a carrying balance of \$240,000, which was FDIC insured.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

3. Cash and Investments (continued)

Investments

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

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.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

3. Cash and Investments (continued)

As of December 31, 2010, the District had the following investments:

Investment	Maturity	<u>Fair Value</u>
	Weighted average	
Colorado Surplus Asset Trust Fund (CSAFE)	under 60 days	<u>\$ 2,302,630</u>

CSAFE

During 2010, 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, 2010, the District had \$2,302,630 invested in CSAFE.

Cash and investments as of December 31, 2010 are classified in the accompanying financial statements as follows:

	<u>2010</u>
Equity in Pooled Cash - Unrestricted	\$ 109,246
Equity in Pooled Cash - Restricted	<u>2,433,384</u>
	<u>\$ 2,542,630</u>

4. Long-Term Capital and Service Obligations Receivable

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, 2010.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

5. Long-Term Liabilities

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.

The following is an analysis of changes in the District's long-term debt for the year ended December 31, 2010:

	Balance December 31, 2009	Additions	Payments	Balance December 31, 2010	Due Within One Year
Series 2010A, \$5,200,000					
Revenue Bonds	\$ -	\$ 5,200,000	\$ -	\$ 5,200,000	\$ -
Series 2010B, \$17,000,000					
Revenue Bonds	<u>-</u>	<u>17,000,000</u>	<u>-</u>	<u>17,000,000</u>	<u>-</u>
	<u>\$ -</u>	<u>\$ 22,200,000</u>	<u>\$ -</u>	<u>\$ 22,200,000</u>	<u>\$ -</u>

The detail of the District's long-term debt outstanding at December 31, 2010 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.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

5. Long-Term Liabilities (continued)

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

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2011	\$ -	\$ 399,822	\$ 399,822
2012	-	416,000	416,000
2013	-	416,000	416,000
2014	-	416,000	416,000
2015	5,000	416,000	421,000
2016-2020	80,000	2,069,600	2,149,600
2021-2025	300,000	2,008,400	2,308,400
2026-2030	660,000	1,834,800	2,494,800
2031-2035	1,185,000	1,493,600	2,678,600
2036-2040	2,970,000	906,800	3,876,800
Total	<u>\$ 5,200,000</u>	<u>\$ 10,377,022</u>	<u>\$ 15,577,022</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 expires on December 1, 2011 but will 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 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, 2010

5. Long-Term Liabilities (continued)

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>
2011	\$ -	\$ 343,400	\$ 343,400
2012	-	343,400	343,400
2013	-	343,400	343,400
2014	-	343,400	343,400
2015	-	343,400	343,400
2016-2020	-	1,717,000	1,717,000
2021-2025	690,000	1,689,528	2,379,528
2026-2030	1,475,000	1,561,763	3,036,763
2031-2035	1,955,000	1,384,003	3,339,003
2036-2040	2,540,000	1,152,511	3,692,511
2041-2046	<u>10,340,000</u>	<u>570,044</u>	<u>10,910,044</u>
Total	<u>\$ 17,000,000</u>	<u>\$ 9,791,849</u>	<u>\$ 26,791,849</u>

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

5. Long-Term Liabilities (continued)

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, 2010:

	Authorized November 2, 2004	Authorization Used, Series 2010	Remaining at December 31, 2010
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.

6. Net Assets

Restricted assets include net assets 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 assets as of December 31, 2010 totaled \$(27,214,703).

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

7. Related Parties

The 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.). The members of the Board of Directors are officers, employees or associated with the Developer and may have conflicts of interest in dealing with the District.

8. Risk Management

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.

9. Intergovernmental Agreements

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.

Cornerstone Metropolitan District No. 2
Notes to Financial Statements (continued)
December 31, 2010

10. Tax, Spending and Debt Limitations

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, 2010, 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.

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, 2010

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
Revenue:				
Property taxes	\$ 725,000	\$ 725,000	\$ 715,535	\$ (9,465)
Specific ownership taxes	53,860	53,860	48,074	(5,786)
Investment income	1,000	1,000	1,156	156
Total Revenue	<u>779,860</u>	<u>779,860</u>	<u>764,765</u>	<u>(15,095)</u>
Expenditures:				
General government				
Operations transfer to				
Cornerstone Metro Dist. No. 1	272,314	272,314	267,291	5,023
Capital transfer to				-
Cornerstone Metro Dist. No. 1	486,276	486,276	477,305	8,971
Treasurer's fees	20,270	20,270	20,119	151
Contingency	1,000	1,000	-	1,000
Debt service				-
Letter of credit fees	-	-	28,421	(28,421)
Bond interest	-	-	2,768	(2,768)
Bond issuance costs	-	495,309	496,105	(796)
Total Expenditures	<u>779,860</u>	<u>1,275,169</u>	<u>1,292,009</u>	<u>(16,840)</u>
Excess Revenue Over (Under)				
Expenditures	<u>-</u>	<u>(495,309)</u>	<u>(527,244)</u>	<u>(31,935)</u>
Other financing sources (uses):				
Bond proceeds	-	22,200,000	22,200,000	-
Intergovernmental transfer to				
Cornerstone Metro Dist. No. 1	-	(19,511,388)	(19,503,673)	7,715
Development fees	-	218,583	217,383	(1,200)
Intergovernmental contribution	-	15,000	15,779	779
Total other financing sources (uses)	<u>-</u>	<u>2,922,195</u>	<u>2,929,489</u>	<u>7,294</u>
Change in fund balance	-	2,426,886	2,402,245	(24,641)
Fund Balance—Beginning of year	<u>335</u>	<u>303</u>	<u>303</u>	<u>-</u>
Fund Balance—End of Year	<u>\$ 335</u>	<u>\$ 2,427,189</u>	<u>\$ 2,402,548</u>	<u>\$ (24,641)</u>