HIGHLANDS RANCH METROPOLITAN DISTRICT
FINANCE WORKSHOP ADDENDA

February 22, 2017

Addendum documents can also be viewed at
http://highlandsranch.org
or
http://intranet.highlandsranch.org/default.aspx

- The PFM Group
- HRMD Financial Results as of December 2016
Highlands Ranch Metropolitan District
Investment Performance Review
Quarter Ended December 31, 2016

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Economic and Market Update

CURRENT MARKET THEMES

- Treasury yields are much higher and the yield curve is steeper as long-term rates soared with higher inflation expectations post-election
- Market participants expect the Federal Reserve (the "Fed") to raise rates twice in 2017 under moderate economic conditions:
  - GDP growth accelerating after weak first half of 2016
  - Labor market continues to strengthen
  - Inflation picking up slowly
- Fed officials forecast three interest rate hikes, according to the "dot plot"
- President-elect Trump's proposed spending policies are expected to drive inflation higher and may benefit corporations through tax cuts and deregulation
- Upcoming 2017 elections in Europe could add political uncertainty and generate market volatility

U.S. ECONOMIC & MARKET HIGHLIGHTS

Over the Last 12 Months

<table>
<thead>
<tr>
<th>Economic Highlights</th>
<th>Market Highlights</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer Prices</td>
<td>U.S. Real GDP</td>
</tr>
<tr>
<td>Highest since 2015</td>
<td>Highest since 2015</td>
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<tr>
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<td>Highest since 2016</td>
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U.S. ECONOMY BOUNCES BACK IN THIRD QUARTER

- U.S. GDP growth increased at an annual rate of 3.5% in the third quarter of 2016, the strongest reading in two years.
- Third quarter GDP reflected positive contributions from personal consumption, gross private investment, government spending, and net exports. Gross private investment has returned to positive territory, driven entirely by a large increase in private inventories, after three straight quarters of negative contributions to GDP.

CONSUMER CONFIDENCE

- Consumer confidence surged to the highest level since 2001 following the U.S. presidential election.
- Stronger consumer sentiment should encourage more spending. The recent trend of declining savings rate could also result in even higher personal consumption in 2017.
The U.S. labor market added 156,000 jobs in December, and averaged 180,000 per month in 2016.

- The core personal consumption expenditures ("PCE") price index, the Fed's preferred gauge of core inflation, stayed around 1.7% year-over-year through November, continuing to modestly undershoot the Fed's 2% target.

- The unemployment rate ticked up to 4.7% while the U6 unemployment rate, which includes part-time and discouraged workers for economic reasons, ticked down to 7.4%, the lowest since 2008.

- Average hourly earnings grew at 2.9% for the year, the strongest since 2009.

- Job gains have been solid in recent months and the labor market has continued to strengthen and that economic activity has been expanding at a moderate pace since mid-year.

- Information received since the FOMC (the "Committee") met in November indicates that the labor market has continued to strengthen and that economic activity has been expanding at a moderate pace since mid-year.

- A tightening labor market together with President-elect Trump's proposed spending policies could add to price pressures and prompt the Fed to raise rates faster.

- In view of realized and expected labor market conditions and inflation, the Committee decided to raise the target range for the federal funds rate to 0.50 – 0.75%.

- All 10 voting members of the FOMC supported the monetary policy action.

- The stance of monetary policy remains accommodative, thereby supporting further strengthening in labor market conditions and a return to 2 percent inflation.

- Treasury rates have surged following the U.S. elections, with longer maturities rising substantially due to higher inflation expectations from the President-elect's proposed fiscal policies. The shorter end of the curve also moved higher as market participants priced in a December rate hike.

- As a result, the yield curve has steepened significantly, even compared to a year ago.

- The core personal consumption expenditures ("PCE") price index, the Fed's preferred gauge of core inflation, remained around 1.7% year-over-year through November, continuing to modestly undershoot the Fed's 2% target.

- However, inflation expectations are rising, with market expectations for inflation over the next five years recovering back to levels last seen in 2016, suggesting labor market tightness and President-elect Trump's proposed spending policies could add to price pressures and prompt the Fed to raise rates faster.

- The Fed’s Long Term Inflation Target is 2.0%.

- The average hourly earnings grew at 2.9% for the year, the strongest since 2009.

- The unemployment rate ticked up to 4.7% while the U6 unemployment rate, which includes part-time and discouraged workers for economic reasons, ticked down to 7.4%, the lowest since 2008.

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**COMPONENTS OF TOTAL RETURN**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Return</th>
<th>Income Return</th>
<th>Price Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>10.00%</td>
<td>2.00%</td>
<td>-2.00%</td>
</tr>
<tr>
<td>2004</td>
<td>8.00%</td>
<td>2.00%</td>
<td>-4.00%</td>
</tr>
<tr>
<td>2005</td>
<td>6.00%</td>
<td>2.00%</td>
<td>-2.00%</td>
</tr>
<tr>
<td>2006</td>
<td>4.00%</td>
<td>2.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>2007</td>
<td>2.00%</td>
<td>2.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>2008</td>
<td>0.00%</td>
<td>2.00%</td>
<td>-4.00%</td>
</tr>
<tr>
<td>2009</td>
<td>-2.00%</td>
<td>2.00%</td>
<td>-4.00%</td>
</tr>
<tr>
<td>2010</td>
<td>2.00%</td>
<td>2.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>2011</td>
<td>2.00%</td>
<td>2.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>2012</td>
<td>4.00%</td>
<td>2.00%</td>
<td>2.00%</td>
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<tr>
<td>2013</td>
<td>6.00%</td>
<td>2.00%</td>
<td>4.00%</td>
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<tr>
<td>2014</td>
<td>8.00%</td>
<td>2.00%</td>
<td>6.00%</td>
</tr>
<tr>
<td>2015</td>
<td>10.00%</td>
<td>2.00%</td>
<td>8.00%</td>
</tr>
<tr>
<td>2016</td>
<td>12.00%</td>
<td>2.00%</td>
<td>10.00%</td>
</tr>
</tbody>
</table>

**MONEY MARKET REFORM TAKES HOLD**

- SEC-imposed money market reforms, which became effective in October 2016, caused a significant shift in assets from prime funds (which typically purchase short-term instruments) to government-only funds.

- As a result, yields widened sharply, especially in the 6-12 month area of the curve, making commercial paper and negotiable book certificates (“CDs”) attractive alternatives to Treasury bills and short-term agency securities.

**YIELD ENVIRONMENT**

<table>
<thead>
<tr>
<th>Maturity</th>
<th>Treasury</th>
<th>Federal Agency</th>
<th>AA Corporate</th>
<th>A Corporate</th>
<th>AAA/Treasury</th>
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</thead>
<tbody>
<tr>
<td>3-Month</td>
<td>0.50%</td>
<td>0.54%</td>
<td>0.62%</td>
<td>0.56%</td>
<td>0.51%</td>
</tr>
<tr>
<td>6-Month</td>
<td>0.61%</td>
<td>0.64%</td>
<td>1.07%</td>
<td>1.29%</td>
<td>1.20%</td>
</tr>
<tr>
<td>1-Year</td>
<td>0.81%</td>
<td>0.85%</td>
<td>1.30%</td>
<td>1.42%</td>
<td>1.26%</td>
</tr>
<tr>
<td>2-Year</td>
<td>1.11%</td>
<td>1.25%</td>
<td>1.41%</td>
<td>1.60%</td>
<td>1.50%</td>
</tr>
<tr>
<td>3-Year</td>
<td>1.45%</td>
<td>1.38%</td>
<td>1.91%</td>
<td>2.13%</td>
<td>1.77%</td>
</tr>
<tr>
<td>5-Year</td>
<td>1.53%</td>
<td>2.05%</td>
<td>2.42%</td>
<td>2.62%</td>
<td>2.24%</td>
</tr>
<tr>
<td>10-Year</td>
<td>2.45%</td>
<td>2.83%</td>
<td>3.28%</td>
<td>3.37%</td>
<td>3.10%</td>
</tr>
</tbody>
</table>

**POTENTIAL IMPACT OF A TRUMP ADMINISTRATION**

**Fiscal**
- Massive infrastructure spending
- Increased military spending
- Entitlement changes (but not social security)

**Monetary**
- Fill 2 vacancies on Federal Reserve Board
- Increase Congressional oversight of Fed
- Replace chair and vice chair when terms expire in February 2018

**Regulatory**
- Reduce corporate and personal income taxes
- Simplify, not cut
- Repellent stock
- Eliminate future limits on financial services

**Immigration**
- Restrict immigration
- Deport undocumented immigrants
- Force Mexico to pay

**Trade**
- Challenge current trade policy
- Renegotiate NAFTA, abandon TPP
- Impose tariffs on steel to pressure nations to negotiate bilateral agreements

**2017 OUTLOOK: SUMMING IT ALL UP**

**Key Takeaways:**
- U.S. economy expected to show improving growth
- Interest rates are likely to continue rising at modest pace
- Inflation will rise from historic lows
- 35-year bull market in bonds likely over

**Upside Opportunity:**
- Faster economic growth creates a virtuous cycle of improving productivity and lower deficits, boosting equities and bonds

**Downside Risks:**
- Rising political uncertainty around the world
- Increasing trade frictions
- Business cycle is long in duration

**Fixed Income Portfolio Strategy Implications**
- Return drivers by FOMC policy and economic landscape
- Remaining tailwinds in the bond market due to political uncertainty
- Sector allocation remains broadly diversified
- Continued emphasis on use of cash and other spread products

**Portfolio Characteristics and Investment Strategy**
PORTFOLIO RECAP

- The Highlands Ranch Metro District (HRMD) portfolio is designed to generate positive returns over the long term by investing in a diversified mix of fixed-income securities. The portfolio is managed to achieve a satisfactory level of total return, consistent with the HRMD's investment objectives.

- The portfolio's credit quality is rated by Standard & Poor's (S&P) and Moody's Investors Service (Moody's). The portfolio's credit quality is currently rated A-1 by S&P and A3 by Moody's.

Portfolio Stats

- Portfolio/Benchmark Duration 12/31/16 09/30/16 06/30/16 03/31/16 1 Year 3 Year 5 Year
- Paper: 5.0% 4.0% 7.3% 7.3% 4.0% 3.8% 3.8%
- Corporate: 13.1% 10.5% 13.1% 13.1% 13.1% 13.1% 13.1%
- U.S. Treasury: 68.3% 63.1% 61.6% 61.6% 61.6% 61.6% 61.6%
- Supra-Natl Agency: 9.0% 7.5% 9.0% 9.0% 9.0% 9.0% 9.0%
- Federal Agency/GSE: 0.9% 0.7% 0.9% 0.9% 0.9% 0.9% 0.9%
- Other: 0.1%

For much of the past year, we maintained a duration position close to the duration of the portfolio's performance benchmark. By late October, however, we recognized that the uncertainty related to the election, and the strong likelihood of a Fed rate increase, had created an environment less favorable to this duration position. We strategically shortened portfolio durations in late October, reducing the price sensitivity of portfolios to interest rate changes as shorter durations are better for portfolios in a rising rate environment. Then, in early December, following the dramatic rise in interest rates, we extended durations to be more closely aligned with benchmarks, capturing the higher yields available.

- The well-publicized reforms to the money market fund industry took effect in the fourth quarter. The reforms caused significant changes in market conditions, leading to increased demand for government funds, that hold only government securities. The result was increased demand for—and thus lower yields on—short-term government securities and reduced demand for—and thus higher yields on—short-term credit instruments (e.g., commercial paper and bank CDs).

- We will continue to monitor incoming economic data, Fed policy, and market relationships, adjusting portfolio positioning as needed. This will contribute to maintaining overall performance and enhancing market value.

INVESTMENT STRATEGY OUTLOOK

Although economic growth has been relatively strong in 2017, we expect a modest uptick in economic growth in the U.S., a modest increase in inflation, and continued low interest rates in the U.S. market.

- The most recent Federal Open Market Committee (FOMC) projections indicate three Fed rate hikes in 2017 and another three hikes in 2018. The market's new consensus, as of year-end, is for a rate of 1.62% in December 2017.

- The market remains bullish on the Trump administration's potential for increasing economic growth in the U.S. through increased corporate spending, lower taxes, and reduced regulations. As a result, we expect strong growth in earnings and profits in 2017.

- Corporate earnings growth, which significantly lagged behind GDP growth in recent years due to the significant impact of lower oil prices on a number of sectors, has far exceeded market expectations in 2017. Professional forecasts for corporate earnings growth in 2018 are expected to be 8%.

- Our strategy continues to favor broad allocation to various credit sectors, including corporate notes, commercial paper, negotiable bank CDs, and asset-backed securities. We will continue to monitor incoming economic data, Fed policy, and market relationships, adjusting portfolio positioning as needed. This will contribute to maintaining overall performance and enhancing market value.
<table>
<thead>
<tr>
<th>Security Type</th>
<th>Sub-Total</th>
<th>Value at Cost</th>
<th>Dated Date/Coupon/Maturity</th>
<th>CUSIP</th>
<th>Par</th>
<th>Rating</th>
<th>Rating</th>
<th>Accrued</th>
<th>Amortized</th>
<th>Market</th>
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<tr>
<td>U.S. Treasury Notes</td>
<td>$38,815,000.00</td>
<td>$39,003,884.15</td>
<td>1.12%</td>
<td>$121,118.88</td>
<td>$38,906,968.40</td>
<td>$38,748,231.84</td>
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<td>DTD 02/12/2014 1.950% 02/12/2019</td>
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<td>$374,336.25</td>
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<td>$374,932.57</td>
<td>1.09</td>
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<td>$374,921.25</td>
<td>$375,078.91</td>
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</table>
ACCRUED INTEREST: Interest that is due on a bond or other fixed income security since the last interest payment was made.

AGENCIES: Federal agency securities and/or Government-sponsored enterprises.

AMORTIZED COST: The original cost of the principal of the security is adjusted for the amount of the periodic reduction of any discount or premium from the purchase date until the date of the report. Discount or premium with respect to short term securities (those with less than one year to maturity at time of issuance) is amortized on a straight line basis. Such discount or premium with respect to longer term securities is amortized using the constant yield basis.

BANKERS' ACCEPTANCE: A draft or bill or exchange accepted by a bank or trust company. The accepting institution guarantees payment of the bill, as well as the insurer.

COMMERCIAL PAPER: An unsecured obligation issued by a corporation or bank to finance its short-term credit needs, such as accounts receivable and inventory.

CONTRIBUTION TO DURATION: Represents each sector or maturity range's relative contribution to the overall duration of the portfolio measured as a percentage weighting. Since duration is a key measure of interest rate sensitivity, the contribution to duration measures the relative amount or contribution of that sector or maturity range to the total rate sensitivity of the portfolio.

DURATION TO WORST: A measure of the sensitivity of a security's price to a change in interest rates, stated in years, computed from cash flows to the maturity date or to the put date, whichever results in the highest yield to the investor.

EFFECTIVE DURATION: A measure of the sensitivity of a security's price to a change in interest rates, stated in years.

EFFECTIVE YIELD: The total yield an investor receives in relation to the nominal yield or coupon of a bond. Effective yield takes into account the power of compounding on investment returns, while nominal yield does not.

FDIC: Federal Deposit Insurance Corporation. A federal agency that insures bank deposits to a specified amount.

INTEREST RATE: Interest per year divided by principal amount, expressed as a percentage.

MARKET VALUE: The value that would be received or paid for an investment in an orderly transaction between market participants at the measurement date.

MATURITY: The date upon which the principal or stated value of an investment becomes due and payable.

NEGOTIABLE CERTIFICATES OF DEPOSIT: A CD with a very large denomination, usually $1 million or more that can be traded in secondary markets.

PAR VALUE: The nominal dollar face amount of a security.

PASS THROUGH SECURITY: A security representing pooled debt obligations that passes income from debtors to its shareholders. The most common type is the mortgage-backed security.

REPURCHASE AGREEMENTS: A holder of securities sells these securities to an investor with an agreement to repurchase them at a fixed price on a fixed date.

SETTLE DATE: The date on which the transaction is settled and monies/securities are exchanged. If the settle date of the transaction occurs on a non-business day (i.e. coupon payments and maturity proceeds), the funds are exchanged on the next business day.

TRADE DATE: The date on which the transaction occurred however the final consummation of the security transaction and payment has not yet taken place.

UNSETTLED TRADE: A trade which has been executed however the final consummation of the security transaction and payment has not yet taken place.

U.S. TREASURY: The department of the U.S. government that issues Treasury securities.

YIELD: The rate of return based on the current market value, the annual interest receipts, maturity value and the time period remaining until maturity, stated as a percentage, on an annualized basis.

YTM AT COST: The yield to maturity at cost is the expected rate of return, based on the original cost, the annual interest receipts, maturity value and the time period from purchase date to maturity, stated as a percentage, on an annualized basis.

YTM AT MARKET: The yield to maturity at market is the rate of return, based on the current market value, the annual interest receipts, maturity value and the time period remaining until maturity, stated as a percentage, on an annualized basis.
### Revenues

<table>
<thead>
<tr>
<th>Department</th>
<th>2015</th>
<th>2016</th>
<th>2016 Budget</th>
<th>2017 Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property Tax (Total)</td>
<td>2,360,000</td>
<td>2,400,000</td>
<td>2,450,000</td>
<td>2,600,000</td>
</tr>
<tr>
<td>Specific Ownership</td>
<td>3,010,000</td>
<td>3,050,000</td>
<td>3,100,000</td>
<td>3,150,000</td>
</tr>
<tr>
<td>System Development Fees</td>
<td>2,620,000</td>
<td>2,660,000</td>
<td>2,700,000</td>
<td>2,740,000</td>
</tr>
<tr>
<td>Total</td>
<td>7,990,000</td>
<td>8,080,000</td>
<td>8,250,000</td>
<td>8,390,000</td>
</tr>
</tbody>
</table>

### Property Tax Revenues

- Program based revenues
- Mansion
  - Upper level home sales conservation
- Recreation 91.1%
- Youth Programs under 30%
- Adult Programs under 50%
- Conservation Trust
- Lottery Proceeds $553k
- 5 year average proceeds $465k
- Other
- Cell Site leases, insurance proceeds, grants

### Specific Ownership Tax

- 2016 Budget - $1,890,000
- YTD Actual - $2,373,000
- Projection - $2,300,000
- 2017 Budget $2,000,000

### General Fund Expenditure Chart

- Contracted Services: $1,230,000
- Fixed Based Capital: $16,000,000
- Total Noncapital: $17,230,000
- Total Expenditures: $33,560,000

- Miscellaneous Outside Services (Community Relations)
  - Outside budget $9,500,000
  - Water: signals over budget $2,500

### Revenues - Unaudited

<table>
<thead>
<tr>
<th>Department</th>
<th>2015</th>
<th>2016</th>
<th>2016 Budget</th>
<th>2017 Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property Tax</td>
<td>2,400,000</td>
<td>2,440,000</td>
<td>2,490,000</td>
<td>2,540,000</td>
</tr>
<tr>
<td>SOT</td>
<td>692,000</td>
<td>695,000</td>
<td>698,000</td>
<td>701,000</td>
</tr>
<tr>
<td>Development Fees</td>
<td>3,000,000</td>
<td>3,050,000</td>
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<td>3,150,000</td>
</tr>
<tr>
<td>Program Revenues</td>
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<td>1,450,000</td>
<td>1,500,000</td>
<td>1,550,000</td>
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<tr>
<td>Utilities</td>
<td>2,750,000</td>
<td>2,800,000</td>
<td>2,850,000</td>
<td>2,900,000</td>
</tr>
<tr>
<td>Other</td>
<td>1,500,000</td>
<td>1,550,000</td>
<td>1,600,000</td>
<td>1,650,000</td>
</tr>
</tbody>
</table>

### Total Revenues

- 2016 Revenues $56.7M, 99% of budgeted revenues $70.3M
## Recreation & Park Services

### Budget Breakdown

<table>
<thead>
<tr>
<th>Category</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recreation Programs</td>
<td>$1,113,130</td>
<td>$1,210,703</td>
<td>$1,067,095</td>
<td>$1,180,122</td>
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<tr>
<td>Senior Services</td>
<td>$72,463</td>
<td>$79,900</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Park Services</td>
<td>$669,383</td>
<td>$750,494</td>
<td>$666,448</td>
<td>$794,633</td>
</tr>
</tbody>
</table>

### Revenue

- Operations Budget: (Expenses - Revenue) $222,625
- Other Revenue: $329,197
- Revenue from Reservations: $319,968
- Revenue from Recreation/Park Services: $454,170

### Expenditures

- General Fund Transfers: (Budget - Expenditures) $222,625
- Senior Services: $329,197
- Recreation/Park Services: $454,170

### Financial Summary

- **Fund Balance - Beginning**: -
- **Fund Balance - Ending**: $4,200,326
- **Revenue and Other Financing Uses**: $101,694

### Notes

- Lower than budgeted revenue is offset by lower than budgeted expenditures.
- Adopted 2016 budget included Senior Services in Operations transferred mid-year to Recreation.
- General Fund Support increase from 2015 of $307,225 (48%).

---

## Mansion Event Count

### Mansion Full Fee Events

<table>
<thead>
<tr>
<th>Year</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total</strong></td>
<td><strong>38</strong></td>
<td><strong>42</strong></td>
<td><strong>37</strong></td>
<td><strong>43</strong></td>
<td><strong>58</strong></td>
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<tr>
<td><strong>Community Events</strong></td>
<td><strong>20</strong></td>
<td><strong>23</strong></td>
<td><strong>19</strong></td>
<td><strong>22</strong></td>
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<tr>
<td><strong>HRCA Events</strong></td>
<td><strong>16</strong></td>
<td><strong>19</strong></td>
<td><strong>18</strong></td>
<td><strong>21</strong></td>
<td><strong>33</strong></td>
</tr>
<tr>
<td><strong>Mansion Events</strong></td>
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<td><strong>3</strong></td>
<td><strong>2</strong></td>
<td><strong>3</strong></td>
<td><strong>2</strong></td>
</tr>
</tbody>
</table>

**Community Events including:****
- Mother's Day Brunch
- HRCA events
- Valentine's Day