



**Financial Statements  
June 30, 1999 and 1998  
(With Independent Auditors' Report Thereon)**

**City of Houston Reinvestment Zone No. 1**

Report No. 00-04



OFFICE OF THE CITY CONTROLLER  
CITY OF HOUSTON  
TEXAS

SYLVIA R. GARCIA

July 14, 2000

The Honorable Lee P. Brown, Mayor  
City of Houston, Texas

SUBJECT: City of Houston Reinvestment Zone No. 1  
Financial Statements – June 30, 1999 and 1998


Dear Mayor Brown:

In accordance with the City's contract with KPMG, KPMG has completed an audit of the combined balance sheets of the Reinvestment Zone No. 1, City of Houston, Texas (the Zone) as of June 30, 1999 and 1998 and the combined statements of revenues, expenditures and changes in fund balances for the years then ended.

Their statements, attached for your review, noted that the financial statements present fairly, in all material respects, the financial position of the Zone, as of June 30, 1999 and 1998, and the results of its operations for the years then ended in conformity with generally accepted accounting principles. Draft copies of the statements were provided to City officials and Mr. David Hawes, the Zone Administrator.

We appreciate the cooperation extended to the KPMG auditors by City personnel during the course of the audit.

Respectfully submitted,

  
Sylvia R. Garcia  
City Controller

xc: City Council Members  
Albert Haines, Chief Administrative Officer  
Cheryl Dotson, Chief of Staff, Mayor's Office  
Robert Litke, Director, Planning and Development Department  
Sara Culbreth, Acting Director, Finance and Administration Department  
David Hawes, Zone Administrator, Hawes, Hill & Patterson, Consultants

## Independent Auditors' Report

The Board of Directors  
Reinvestment Zone No. 1,  
City of Houston, Texas  
Houston, Texas:

We have audited the accompanying combined balance sheets of the Reinvestment Zone No. 1, City of Houston, Texas (the Zone) as of June 30, 1999 and 1998 and the combined statements of revenues, expenditures and changes in fund balances for the years then ended. These financial statements are the responsibility of the Zone's management. Our responsibility is to express an opinion on financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits 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 audits provide a reasonable basis for our opinion.

As discussed in note 2, the financial statements present only Reinvestment Zone No. 1, City of Houston, Texas, which is a discretely presented component unit, and are not intended to present fairly the financial portion of the City of Houston, Texas, and the results of operations and the cash flows of its propriety fund types and nonexpendable trust funds in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Zone, as of June 30, 1999 and 1998, and the results of its operations for the years then ended in conformity with generally accepted accounting principles.

KPMG LLP

March 31, 2000

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Combined Balance Sheets - All Fund Types and Account Groups  
June 30, 1999 and 1998

	1999				1998			
	Governmental Fund Type		General Long-Term Debt Account Group	Totals (memorandum only)	Governmental Fund Type		General Long-Term Debt Account Group	Totals (memorandum only)
	General	Capital Projects			Debt Service	General		
<b>Assets and Other Debits</b>								
Investments	211,283	176,567	-	615,850	137,722	171,036	-	536,758
Tax increment receivable	50,741	-	-	50,741	14,104	-	-	14,104
Due from affiliates	4,168	-	-	4,168	30,223	-	-	30,223
Other debits:								
Restricted assets - amount available for debt service			228,000	228,000			228,000	228,000
Amount to be provided for retirement of general long-term debt								
<b>Total assets and other debits</b>	<b>\$ 266,192</b>	<b>176,567</b>	<b>228,000</b>	<b>3,040,759</b>	<b>182,049</b>	<b>171,036</b>	<b>228,000</b>	<b>2,861,085</b>
<b>Liabilities and Fund Equity</b>								
Due to City of Houston	\$ 112,851				125,549			125,549
Due to affiliates	18,084				43,750			43,750
Deferred revenues	50,741				14,104			14,104
Claims and judgments								
Bonds payable								
<b>Total liabilities</b>	<b>181,676</b>	<b>-</b>	<b>2,370,000</b>	<b>2,551,676</b>	<b>183,403</b>	<b>-</b>	<b>2,280,000</b>	<b>2,280,000</b>
Reserved fund balance				228,000			228,000	228,000
Unreserved fund balances - undesignated fund balance	84,516	176,567	-	261,083	(1,354)	171,036	-	169,682
<b>Total liabilities and fund equity</b>	<b>\$ 266,192</b>	<b>176,567</b>	<b>228,000</b>	<b>3,040,759</b>	<b>182,049</b>	<b>171,036</b>	<b>228,000</b>	<b>2,861,085</b>

See accompanying notes to financial statements

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Combined Statements of Revenues, Expenditures and  
Changes in Fund Balances

Years ended June 30, 1999 and 1998

	1999				1998			
	General	Capital Projects	Debt Service	Totals (memorandum only)	General	Capital Projects	Debt Service	Totals (memorandum only)
<b>Revenues:</b>								
Tax increments	335,250	-	-	335,250	207,528	-	-	207,528
Utility revenues	13,200	-	-	13,200	13,200	-	-	13,200
Interest	13,182	5,531	12,688	31,401	10,558	6,309	12,652	29,519
<b>Total revenues</b>		<b>5,531</b>	<b>12,688</b>	<b>379,851</b>	<b>231,286</b>	<b>6,309</b>	<b>12,652</b>	<b>250,247</b>
<b>Expenditures:</b>								
Low income housing	111,750	-	-	111,750	69,176	-	-	69,176
Debt service	-	-	176,700	176,700	-	-	176,700	176,700
<b>Total expenditures</b>	<b>111,750</b>	<b>-</b>	<b>176,700</b>	<b>288,450</b>	<b>69,176</b>	<b>-</b>	<b>176,700</b>	<b>245,876</b>
<b>Other financing sources (uses):</b>								
Operating transfers in	12,688	-	176,700	189,388	12,652	-	176,700	189,352
Operating transfers out	(176,700)	-	(12,688)	(189,388)	(176,700)	-	(12,652)	(189,352)
<b>Total other financing sources (uses)</b>	<b>(164,012)</b>	<b>-</b>	<b>164,012</b>	<b>-</b>	<b>(164,048)</b>	<b>-</b>	<b>164,048</b>	<b>-</b>
<b>Excess (deficiency) of revenues and other financing sources over expenditures</b>	<b>85,870</b>	<b>5,531</b>	<b>-</b>	<b>91,401</b>	<b>(1,938)</b>	<b>6,309</b>	<b>-</b>	<b>4,371</b>
<b>Fund balances before prior period adjustment</b>	<b>(1,354)</b>	<b>171,036</b>	<b>228,000</b>	<b>397,682</b>	<b>54,048</b>	<b>156,515</b>	<b>228,000</b>	<b>438,563</b>
<b>Prior period adjustment due to correction of an error</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(53,464)</b>	<b>8,212</b>	<b>-</b>	<b>(45,252)</b>
<b>Fund balances at beginning of period</b>	<b>(1,354)</b>	<b>171,036</b>	<b>228,000</b>	<b>397,682</b>	<b>584</b>	<b>164,727</b>	<b>228,000</b>	<b>393,311</b>
<b>Fund balances at end of period</b>	<b>\$ 84,516</b>	<b>176,567</b>	<b>228,000</b>	<b>489,083</b>	<b>(1,354)</b>	<b>171,036</b>	<b>228,000</b>	<b>397,682</b>

See accompanying notes to financial statements.

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

**(1) Summary of Significant Accounting Policies**

The following is a summary of the significant accounting policies followed by the Reinvestment Zone No. 1, City of Houston, Texas (the Zone).

**(a) Zone Formation**

In December 1990, the City Council of the City of Houston, Texas adopted an ordinance creating Reinvestment Zone No. 1, City of Houston, Texas (the Zone) pursuant to the provisions of Chapter 311, Texas Tax Code, to promote development or redevelopment in the Zone. The ordinance described the Zone's boundaries, created a Board of Directors, and established the Zone's Tax Increment Fund (TIF) to pay project costs for the Zone, as defined by the Texas Tax Code, or to satisfy the claims of holders of TIF Bonds or notes issued for the Zone. The Zone is located adjacent to the Galleria shopping area, approximately seven miles from the Central Business District of the City. The Zone was enlarged effective January 1, 1993 and covers an area of approximately 115 acres.

**(b) Basis of Presentation - Fund Accounting**

The accounts of the Zone are organized on the basis of funds and an account group. The operations of a fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures.

The following fund type and account group are included in the combined financial statements:

**Governmental Fund Type**

The measurement focus of governmental funds is based upon the determination of changes in current financial resources, rather than net income. Governmental funds include the following fund types:

**General fund** - The general fund is the Zone's primary operating fund. It accounts for all financial resources of the Zone, except those required to be accounted for in another fund.

**Capital projects fund** - The capital projects fund accounts for financial resources to be used for the acquisition or construction of major capital facilities.

**Debt service fund** - The debt service fund accounts for the accumulation of resources for, and the payment of, general long-term debt principal and interest.

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

**Account Group**

- **General long-term debt account group** - The general long-term debt account group accounts for all unmatured general long-term liabilities.

**(c) Basis of Accounting**

The modified accrual basis of accounting is used to account for governmental fund type operations. Under this method of accounting, revenues are recorded when received except for revenues susceptible to accrual, i.e., both measurable and available. Expenditures are generally recorded when the fund liability is incurred and expected to be paid from available resources. Tax increment revenues are not susceptible to accrual under the modified accrual basis of accounting and are recognized on a cash basis.

**(d) Cash and Investments**

All cash is deposited with financial institutions in interest bearing accounts or is invested. The Zone's cash and investments are administered by the City of Houston (the City) using a pooled concept. Interest earnings of the pool are apportioned to the Zone based on its relative share of the cash and investment pool. Amounts on deposit in interest bearing accounts and other investments are displayed on the balance sheet as "investments" and carried at their fair market values.

The Zone's investments are guided by State laws, various City ordinances and the City's investment policy. Authorized investments include direct obligations of the United States or its agencies, certificates of deposit from authorized depository banks (not to exceed 5% of the bank's total deposits), repurchase agreements, and the money-market account at the City's depository bank.

**(e) Encumbrances**

Encumbrances do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year. Unused or unencumbered appropriations lapse at year end.

**(f) Fund Balances**

- **Reserved Fund Balance** - Reserved fund balance is that portion of fund equity, which has been legally segregated for specific purposes.

**Unreserved - Undesignated Fund Balance** - Unreserved - undesignated fund balance is that portion of fund equity, which is available for use in future periods.

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

**(g) Tax Increments**

Pursuant to the City's ordinance establishing the Zone and two intergovernmental agreements with Harris County, Texas (County) and the Houston Independent School District (HISD), the Zone earns a portion of the property taxes levied on each taxing unit's property tax increment over the captured appraised value of real property in the Zone. The captured appraised value is the appraised value of all real property taxable located in the Zone for the year in which the Zone was designated (base year) under Chapter 311 Tax Increment Financing Act of the Texas Property Tax Code.

The base years for the East and West portions of the Zone became effective January 1, 1991 and January 1, 1993, respectively.

Two-thirds of the tax increments are pledged to service principal and interest on long-term debt. One-third of the tax increment is dedicated to providing low-income housing in the City and is set aside in a separate fund not under the Zone's control.

**(h) Provision for Income Taxes**

The Zone qualifies for tax exempt status as a governmental entity. No tax provision is necessary in regard to its excess revenue.

**(i) Financial Statement Total Columns**

Amounts listed in the columns headed "Totals (memorandum only)" on the accompanying combined financial statements are the aggregate of the fund type and account group. No consolidating or other eliminating entries were made in arriving at these amounts, thus, they do not present consolidated information. Accordingly, all total columns in the combined statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis.

**(2) Reporting Entity**

These financial statements include only the activities attributable to the Zone. The Zone is a discretely presented component unit of the City of Houston. Component units are legally separate entities for which the primary government is financially accountable. There are no separate legal entities that are a part of the Zone's reporting entity.

**(3) Investments**

The Zone's investments consist of U.S. Government Securities at June 30, 1999 and 1998. Such securities are categorized as Category 1, which includes investments that are insured or registered or for which the securities are held by the Zone's agent in the Zone's name.



**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

**Long-Term Debt**

Long-term debt outstanding as of June 30, 1999 and 1998 consisted of the following:

Bond issue	Original amount of issue	Bonds payable at June 30, 1999 and 1998
Tax Increment Bonds, (TIF Bonds) Series 1992, 7.75% bonds due on February 1, 2011	\$ 2,280,000	2,280,000

The TIF Bonds are special obligations of the City, solely payable both as to principal and interest and secured by an irrevocable lien on and pledge of the Pledged Revenues to be received from the City's Reinvestment Zone No. 1 (the Zone), as provided in the ordinance authorizing the TIF Bonds (the Bond Ordinance). Pledged revenues consist primarily of two-thirds of the tax increment anticipated to be received from the levy of City, County and HISD ad valorem taxes on certain appraised values, if any, in the Zone.

A schedule of debt service requirements to maturity is as follows:

Year ending June 30,	Principal	Interest	Total
2000	\$ 80,000	,700	
2001	100,000	,500	
2002	100,000	,750	
2003	100,000	,000	
2004	100,000	,250	
Thereafter	1,800,000	,250	
Total	\$ 2,280,000	1,548,450	3,828,450

The Bond Ordinance requires and the Zone has maintained a Bond Reserve Fund in the amount of \$228,000. This amount is recorded in investments in the debt service fund.

**Transactions with the City and Zone Affiliates**

***City of Houston***

The City maintains all accounting records for the Zone for which it receives no payment.

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

The property tax revenues attributable to the assignment of applicable taxes on the City's real property over the captured appraised values for the years ending June 30, 1998 and 1999 were as follows:

	<u>1999</u>	<u>1998</u>
Incremental appraised values:		
Lamar Terrace East	\$ 15,597,170	11,971,890
Lamar Terrace West	3,163,850	151,710
Total revenues	\$ 111,249	78,743

Deferred taxes, which represent taxes levied yet not collected on behalf of the Zone, amount to \$16,015 and \$2,503 as of June 30, 1999 and 1998, respectively.

In December 1992, the Zone entered into a Utility Functions and Service Allocation Agreement with the City. In return for the conveyance of constructed water and sewer infrastructure assets to the City, the Zone receives utility revenues calculated as the difference between retail and contract wholesale rates plus a line maintenance charge. As of June 30, 1999 and 1998, the Zone had \$26,400 and \$13,200, respectively, receivable from the City for utility revenues.

As of June 30, 1999 and 1998, the Zone had \$52,574 and \$(59,177), respectively, payable/(receivable from) to the low-income housing fund.

In addition from time-to-time, the City would advance various cash amounts to the Zone in excess of the tax and utility revenues received/earned. As of June 30, 1999 and 1998, the Zone had \$86,677 and \$197,926, respectively, payable to the City for such advances.

***Harris County***

Pursuant to various agreements, Harris County has agreed to pay the tax increment produced from the collection of taxes on real property located in the City of Houston Reinvestment Zone No. 1 for the period January 1, 1994 through and including the tax year 2010.

The property tax revenues attributable to the assignment of applicable taxes on the County's real property over the captured appraised values for the years ending June 30, 1998 and 1999 were as follows:

	<u>1999</u>	<u>1998</u>
Incremental appraised values:		
Lamar Terrace East (estimated)	\$ 5,627,152	3,368,234
Lamar Terrace West (estimated)	9,384,427	5,429,015
Total revenues	\$ 55,896	33,471

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

Of these total revenues, \$4,168 and \$30,223 remained receivable as of June 30, 1999 and 1998, respectively. As of June 30, 1999 and 1998, \$10,681 and \$4,040, respectively, represent deferred taxes.

***Houston Independent School District***

In December 1996, the Houston Independent School District (HISD) agreed to fully participate in the Zone up to \$0.96 per \$100 of real property assessed value for the period January 1, 1996 through and including the tax year 2010.

The property tax revenues attributable to the assignment of applicable taxes on the HISD's real property over the captured appraised values for the years ending June 30, 1998 and 1999 were as follows:

	1999	1998
Incremental appraised values:		
Lamar Terrace East	\$ 15,089,270	9,437,520
Lamar Terrace West portions	4,138,873	1,188,343
Total revenues	\$ 168,105	95,314

As of June 30, 1999 and 1998, HISD had made payments in excess of calculated revenues and \$18,084 and \$43,750 remained payable to HISD as of June 30, 1999 and 1998, respectively. As of June 30, 1999 and 1998, \$24,045 and \$7,561 represent deferred taxes, respectively.

**(6) Contingencies**

From time to time, the Zone is a defendant in legal proceedings and is aware of pending claims arising in the ordinary course of business. The Zone has recognized a liability of \$90,000 for potential claims and judgements in the General Long-Term Debt Account Group.

**(7) Prior Period Adjustment to Correct Error**

A prior period adjustment has been recorded in the General Fund to recognize utility revenues, amounts due to/from affiliates, and deferred tax increment revenues. In addition, retainage payable and prepaid expenses related to closed contracts were written-off in the Capital Projects Fund.

**(8) Subsequent Event**

On June 9, 1999, an agreement was reached that placed operation of the Zone under the Saint George Redevelopment Authority (the Authority). The agreement consolidates operations and allows the issuance of additional bonds to finance new construction and refinance the Zone's outstanding tax increment bonds.

**REINVESTMENT ZONE NO. 1  
CITY OF HOUSTON, TEXAS**

Notes to Financial Statements

June 30, 1999

The Zone and the Authority entered into an agreement with a developer in September 1999 to reimburse approximately \$2 million in development costs for public improvements and property acquisition for public right-of-way purposes. As of March 31, 2000, the City advanced the Zone approximately \$1 million for reimbursable amounts payable under this agreement. The advance is expected to be repaid pursuant to the agreement discussed below.

Pursuant to a March 29, 2000 agreement with the Zone, the Authority and the City, the City will issue \$5.3 million in certificates of obligation for public improvements and right-of-way acquisition within the Zone. Under this agreement the Zone and the Authority generally agree to reimburse the City for the payment of the developer reimbursement, interest on the certificates, and costs of the public improvements, estimated to total \$6.3 million. The Zone and the Authority have the option of making payments from future bond proceeds issued by the Authority, or in five equal annual installments beginning July 2007.