Financial Internal Audit
of the Sources and Uses of Funds:

# City of Houston Reinvestment Zone No. 1
# and the
# Lamar Terrace Public Improvement Districts
# No. 1 & 2

Report No. 00-05
Inception, November 7, 1990
through June 30, 1999

SYLVIA R. GARCIA

OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

July 14, 2000

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

SUBJECT: Financial Internal Audit of the Sources and Uses of Funds: City of Houston Reinvestment Zone No. 1 and the Lamar Terrace Public Improvement Districts No. 1 and 2 (Report No. 00-05)

Dear Mayor Brown:

In accordance with the City's contract with KPMG, KPMG has completed an internal financial audit of the sources and uses of funds of the City of Houston Reinvestment Zone No. 1, and the Lamar Terrace Public Improvement Districts No. 1 and 2 (collectively referred to as "Lamar Terrace" or "the Zone"). The objective of the audit was to compare the Zone's actual sources and uses of funds from its inception, November 7, 1990 through June 30, 1999 and the Zone's initial stated strategy and plans outlined in the official offering statements for the Zone's outstanding bonds and in the Board minutes.

KPMG's audit procedures included reviewing bond official statements, covenants, City Ordinances, and annual reports; reviewing Board of Directors minutes from inception to date; and analyzing the use of funds on a project and expenditure classification basis from inception through June 30, 1999. Their report is attached for your review. Draft copies of the report 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
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March 31, 2000

Sylvia R. Garcia, City Controller
City of Houston:

We have completed an internal audit to assist you in assessing financial performance of the sources and uses of funds of the City of Houston, Texas, Reinvestment Zone No. 1, the Lamar Terrace Public Improvement District No.1, and Lamar Terrace Public Improvement District No. 2 (collectively referred to as "Lamar Terrace" or "the Zone"). The objective of this audit was to compare the Zone's actual sources and uses of funds from its inception, November 7, 1990, through June 30, 1999 and the Zone's initial stated strategy and plans outlined in the official offering statements for the Zone's outstanding bonds and in the Zone's minutes of its Board.

Our audit procedures consisted of the following:

- Reviewed bond official statements, covenants, City Ordinances, annual reports and other significant agreements.
- Contrasted reported results to adopted Project and Financing Plans.

  Reviewed minutes of the Board of Directors and other meetings from inception to date.
- Analyzed the use of funds on a project and expenditure classification basis from inception through June 30, 1999.
- Performed a trend analysis of appraised property values.
- Reviewed the flow of funds from the participating taxing jurisdictions.
- Interviewed the Zone Administrator, Harris County, Houston Independent School District, and City of Houston personnel charged with duties related to the Zone.

This report summarizes the results of the above procedures to assist you in assessing the financial performance and the accounting for the sources and uses of funds and provides our recommendations that should enhance the Zone's financial and operational controls.

Our procedures were completed as of March 24, 2000 and have not been updated since that date. KPMG is pleased to have assisted the City in completing this internal audit and appreciates the assistance and cooperation of the Zone Administrator as well as many different City of Houston personnel.

KPMG LLP

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# Executive Summary

## Background

Lamar Terrace was the first tax increment reinvestment zone (TIRZ) created in Houston. Lamar Terrace was created in 1990 at the request of a developer who owned approximately one half the land. The 115-acre area is located near the Galleria. Lamar Terrace, once a thriving middle class residential neighborhood built during the post-World War II era with FHA/VA financing, had by the mid 1970's began a progressive decline into a state of disrepair. Some of this decline was attributed to the continuing impact of the surrounding commercial growth of the Galleria area and the construction and widening of the Southwest Freeway. Yet, stated reasons for the area's decline are the expiration of deed restrictions; extensive physical deterioration of both the infrastructure and housing stock; and, an increase in absentee ownership of former residential and real estate speculators lacking a commitment to maintain the quality of the neighborhood. The Zone was created to assist the developer in transforming the blighted area into an upscale residential community. The Developer's market plan was to construct and sell homes in the prices ranging from $250,000 to $350,000. A total of $3.08 million in bonds were issued to pay for infrastructure improvement. The life of the Zone is 40 years with planned tax increment of approximately $11 million.

## Zone Objectives

The goals and objectives of Lamar Terrace according to early planning documents was to:

- increase and stabilize property values through new development;
- encourage the revitalization and redevelopment of Lamar Terrace, as a low density residential neighborhood, with a neighborhood convenience center on Richmond Avenue;
- encourage the removal of blight, deteriorated buildings, and incompatible land uses;
- preserve and enhance a low density neighborhood character;
- provide necessary infrastructure improvements including streets and utilities;
- prevent through and cut-through traffic, which is incompatible with a low density residential area;
- encourage higher density mixed-use development, including multi-family residential and office space along Richmond Avenue;
- provide a safe, walkable pedestrian environment, with low-volume traffic streets, generous sidewalks and appropriate landscaping;

- encourage public safety and crime prevention through the use of Crime Prevention Through Environmental Design (CPTED) site planning and design principles;
- minimize adverse environmental impacts and to encourage design and planning which respects the Urban environment;
- improve the visual quality of the public realm, street, and front yards; and
- promote the general health, safety, and welfare of the community and surrounding areas.

## Project and Financing Plans

The initial plans were substantially incorporated in the Official Statement for the Tax Increment and Public Improvement District Bonds (TIF and PID bonds), that have been the principal financing instruments for the Zone. Approximately $3.08 million dollars in bonds were issued in 1992 for the purpose of:

- constructing or reconstructing water, wastewater and storm drainage and related infrastructure improvements;
- constructing or reconstructing streets and infrastructure improvements;
- paying the initial two years of bond interest;
- establishing a debt reserve fund for the bonds; and
- paying various costs consisting principally of bond issuance, operational and organizational costs.

The TIF bonds were to be repaid from tax revenues generated from the incremental increase in assessed property valuation due to the development of the subdivision. The PID bonds were to be repaid from one-time assessments (capital assessment) assessed upon each parcel of property within the Zone.

In addition, the Official Statement and other documents disclosed additional funding sources and arrangements included in the initial plans as follows:

- The Metropolitan Transit Authority of Harris County Texas (METRO) agreed to finance a portion of the Hidalgo street reconstruction;
- A Service Allocation Agreement was executed with the City of Houston whereby the Zone would receive utility revenues in exchange for ownership rights of the infrastructure assets constructed;
- The Developer would immediately pay the assessments on his parcels (PID #1);
- One-third of the tax increment generated by the Zone was allocated directly to a low-income housing fund of the City of Houston; and

- A reimbursement agreement with the Developer was signed whereby certain development costs associated with the creation and planning for the Zone would be reimbursed.

## Planned versus Reported Performance

The planned construction of infrastructure improvements, as outlined in the Official Statement for the debt issue, did take place largely as planned, with costs exceeding preliminary estimates but within the bond proceeds and amounts presented in the Official Statement. New streets, sidewalks, driveway aprons, fencing, street lights, removal and replacement of utility lines and construction of new utility lines was performed on the east-side of the following thoroughfares; Fayette, Valverde, Navarro, Lampasas, Hidalgo, Fairdale, and McCullouch.

A visual inspection of the Zone confirms the disparity between the East and West Portions of the Zone resulting from the construction taking place exclusively on the East Side. The East Side is teeming with new homes, construction, and streets while the West Side is still largely an area filled with vacant lots, deteriorated housing, and streets in need of repair. Such blighted conditions have caused the West Side property owners to openly complain about the apparent inequity.

The reason for such a disparity between the two sides is readily apparent. The East Side was the original Zone and benefited from the fact that a Developer had already acquired 51% of the property and had a plan in hand to begin redevelopment efforts. In addition, the Zone's original 1992 Project and Financial Plans were focused almost entirely on the East Side, since the West Side was not added to the Zone until 1993 (see Chronology of Events Appendix).

While an operational expense has been assessed on all property owners which delivered increased security, zoning enforcement and provide for operational expenses, the means for making significant capital improvements on the West side through bonds and/or capital assessments were not approved until March 22, 2000. Plans for the West Side have been developed that should provide the means for improvement in years to come. These include the issuance of bonds to fund infrastructure improvements and the execution of reimbursement agreements with developers that have expressed a readiness to build.

A list of the factors that affected planned versus reported performance follows:

- Unplanned expenditures, such as right of way acquisition costs were incurred;
- Capital items such as landscaping and fencing were constructed later than planned:
- Delays in the actual development of the area by private interests had a detrimental impact on planned revenues; and
- For a period of time certain planned revenue streams were delayed, resulting in funding issues for certain capital items and delayed services – and creating cash flow issues early in the Zone's history. It should be noted that most of the delays were planned so as not to overburden the average homeowner residing within the Zone with additional levies.

These factors have resulted in the development of the area at a slower pace that was originally planned. Once again however, the planned construction of infrastructure improvements did take place largely as planned.

## Subsequent Plans

In May of 1997 an Amended Reinvestment Zone Financing Plan was adopted that took into consideration the Zone's historical chain of events and began setting the blue print for future development efforts. The Amended Plan considered such events as the enlargement of the Zone, participation by HISD and Harris County, the creation of PID #2, and the acquisition of a middle school site by HISD. The Amended Plan called for additional water and sewer construction of approximately $1.8 million over three years (1997-99). Based on this financing plan, over the next twenty years the Zone anticipated costs of $1 million for real property assemblage, organizational and operating costs of $830,000, and legal, planning and engineering costs of $405,000.

The Plan was amended again in May of 1999, reflecting proposed changes to zoning ordinances, the master plan of the community and other municipal ordinances. This plan also called for capital improvement costing of approximately $3.75 million to be incurred over the three-year period from 1999 to 2001. In addition, non-capital costs of approximately $900,000 were expected to be incurred over the five-year period through 2003.

On June 9, 1999, an agreement between the Zone and the Saint George Redevelopment Authority (the Authority) was executed that placed operation of the Zone under the oversight of the Authority with the intent to consolidate operations of all the entities under one organization. In addition, the Authority plans to issue additional bonds, which should be used to finance new construction and refinance outstanding bonds.

In August of 1999, the third amended project plan was approved. This Plan called for changes to City ordinances and the community master plan. Capital costs over the three-year period (1999-2001) are expected to be $6.5 million, including $1 million for real property assemblage.

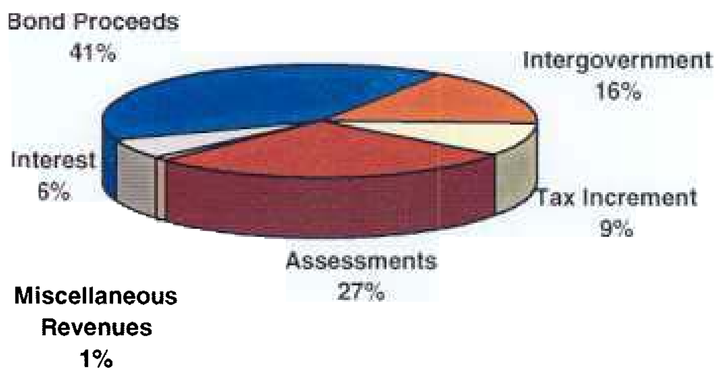
To date the Zone's efforts have substantially been planning and engineering for the design of the West Side. Other expenditures include debt service and management fees. In addition, the Zone entered into an agreement in September 1999, with a Developer to reimburse approximately $2 million in development costs. As of March 31, 2000, the City has funded approximately $1 million on behalf of the Zone under this agreement.

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.

# Sources of Funds

## Funding Sources by Type

The graph below summarizes the Zone's $7.7 million in funding sources by type from inception, November 7, 1990, through June 30, 1999.




The amounts above are substantially derived on a cash basis and do not reflect adjustments necessary to account for revenues on the modified accrual basis. However, such adjustments (primarily tax increments) would not significantly alter the data presented above. A description of each of the funding sources is provided below.

## Bond Proceeds

Bonds were issued to provide the immediate source of funds to begin construction of improvements.

## Tax Increments

As of June 30, 1999, three taxing units — the City of Houston, Harris County, and Houston Independent School District participate in the Zone. The Zone's tax increment revenues for a year represent the tax levied by each respective taxing unit on the current appraised value of real property taxable located in the Zone, less the appraised value of all real property taxable to that unit in their respective base year, multiplied by each taxing unit's participating tax rate. The base year, determined under Chapter 311 of the Tax Increment Financing Act of the Texas Property Tax Code, is the year in which the Zone was designated a reinvestment zone.

*Enlargement of the Zone (January 1, 1993) and Determination of Base Year*

The Zone was enlarged effective January 1, 1993 to incorporate the Westside of the Lamar Terrace subdivision. After this date, the Zone consisted of two portions: Lamar Terrace East (original zone) and Lamar Terrace West. We noted confusion regarding the appropriate base year to use when calculating the tax increments. Based on internal correspondence from the City's legal department, the base year should be determined on the basis of when the area was designated as a tax increment zone. Thus, each portion of the Zone has a distinct base year, East – 1991 and West – 1993.

*Harris County Participation*

Commissioner's Court approved 50% participation in the Zone effective January 1, 1994. The County then approved an increase to 100% participation of tax increment funding, effective January 1, 1996.

*HISD Participation*

The City's Ordinance 97-118 approved an interlocal agreement with HISD whereby HISD agreed to participate in the Reinvestment Zone up to $0.96 per $100 of assessed property valuation. The first payment of increment taxes under the agreement was for the tax year 1996.

*Low Income Housing Fund*

The ordinance creating the Zone specified that one-third of the tax increment revenue would be provided to the City of Houston's low-income housing fund. Subsequent adoption of the ordinance by the County and HISD also committed one-third of the tax increments from those taxing units to the low-income housing fund. During this audit, we noted the payment of taxes to the low-income housing fund had not been applied consistently over the years, resulting in approximately $53,000 being payable from the Zone to the low-income housing fund as of June 30, 1999.

*Accounting for Tax Increments*

Accounting for tax increment payments has been performed through June 30, 1999 on a modified accrual basis, with such tax revenues not being considered susceptible for accrual as defined under Generally Accepted Governmental Accounting Standards. In addition, because tax increments were expected to come in slowly and the Zone was in need of working capital early on, the City advanced tax increment revenues. These advances had not been accurately recorded as liabilities, but have been reconciled and the necessary adjusting entries have been made to the June 30, 1999 financial statements.

The following documents a recalculation of the tax increment revenues and the cash advances/revenue remittances through June 30, 1999.

| June 30, 1999 | Tax Increment collections to date | Remitted to the Zone/Fund | Under (Over) Paid |
|---|---|---|---|
| City of Houston | $ 367,860 | 507,110 | (139,250) |
| Harris County | 138,913 | 134,745 | 4,168 |
| HISD | 360,186 | 378,270 | (18,084) |
| Totals | $ 866,959 | 1,020,125 | (153,166) |
| Revenues: | | | |
| Retained by the Zone | $ 577,972 | 731,139 | (153,166) |
| Paid to Low Income Housing Fund | 288,986 | 288,986 | |
| | $ 866,959 | 1,020,125 | (153,166) |

As shown in the calculations above, the City and HISD have outstanding advances payable by the Zone approximating $139,000 and $18,000, respectively. Harris County owed monies of approximating $4,100 to the Zone.

It should be noted that tax rolls are updated annually and calculations are performed retroactively back five years. This methodology should capture delinquent tax collections made over a rolling five-year period.

During our recalculation of revenues we determined both Harris County and HISD used different base years and/or did not segregate the Zone into East and West portions. In addition, we noted that the tax increment calculation process will be updated shortly and therefore recommend the Zone communicate with all participating taxing units to ensure consistent calculations.

## Assessments

### *PID #1*

The initial Service and Assessment Plan for PID #1 called for a one-year capital assessment levy and an annual operational expense assessment over a four-year period (1992-1996). Each is discussed in more detail below.

*Capital Assessment Levy*

In connection with the issuance of the PID Bonds, a one-time assessment, of $1.12 per square foot — averaging approximately $7,430 per parcel was assessed on each parcel of property within PID #1. Property owners had several payment options — payment in installments over an 11-year period or pay at any time. However, all owners must pay the assessment in full upon the sale of each parcel. The adopted assessment totaled $1,567,728.

The unpaid portion of the assessment was to bear interest at a rate of ½% over the rate of the PID Bonds. Interest was to be billed annually and was due on November 1 of each year. Actual billings are sent out by F&A's Property Lien Group.

*Developer's Assessment*

Included in the Original Financing Plan and Bond Issuance, the Developer (owned 51% of the parcels within the District) agreed and paid assessments on all parcels owned by him upon levy of the assessments by the City. This amount totaled $773,482.

*Operational Expense Assessment*

In the second year of the District's Service and Assessment Plan, an additional assessment plan of $.05 per square foot was proposed to fund operational expenses, but was not authorized. However, the intent of this assessment was later adopted under PID #2 as the Assessment for Supplemental Services.

**PID #2**

The following is a summary of planned assessments pursuant to the Initial Service and Assessment Plan for PID #2.

*Assessment for Supplemental Services*

This assessment was adopted as one of three parts included in the adopted Service and Assessment Plan with the intention of financing supplemental services. Supplemental services included constable contract services, enhanced code enforcement, administration of development regulations, Board management, annual maintenance service, and Zone administrative expenses. An assessment of $.08 per square foot annually for each lot or parcel over five years was approved. Anticipated revenues were projected at $1,201,365. This assessment was adopted by the City on September 18, 1996, Ordinance 96-963.

*Western Redevelopment Area Assessments*

A one-time assessment intended to finance the Western Redevelopment Area Improvements was to be assessed on all property owners in that area. The exact amount of the assessment was to be based on the total cost of the improvements. This assessment has not been levied.

*Perimeter Fence Assessment*

This assessment is the third part of the service and assessment plan and was intended to finance the construction of a perimeter fence at an estimated cost of $400,000. This assessment has not been levied.

## Miscellaneous Revenues

Included in Miscellaneous Revenues are Utility (67%) and Building Permit Revenues (33%).

*Utility Revenues (Service Allocation Agreement)*

An agreement between the City and Zone was reached December 9, 1992 whereby the water and sewer services were to be sold to the Zone at wholesale rates in return for conveyance of the infrastructure assets. The Zone could then sell the services to inhabitants of the Zone at retail netting a profit that could be used to retire the bonds.

During our auditing of the sources and uses of funds we noted that the Zone had not recorded utility revenues for the last several years. Based on discussions with the Public Works & Engineering Department and the Controllers Office, turnover of personnel several years ago resulted in a failure to perform the necessary calculation and record the Zone's utility revenues. Based on recent calculations performed by the City's Department of Public Works and Engineering, utility revenues were computed to total $83,913 from the Zone's inception.

*PID #2 Building Permit Revenues*

Building permit revenues are credited to the Zone as new construction begins. Miscellaneous revenues of approximately $2,000 have been recorded on PID #1's accounting records that, according to the Zone Administrator, belong to PID #2.

## Interest

Interest is earned on the Zone's share of pooled cash and investments. This is recorded in conjunction with the citywide interest apportionment program, which interfaces with the Zone's general ledger.

## Inter-Governmental Revenues

Intergovernmental revenues are derived from three principal sources — an interlocal agreement with METRO, tax increments which were discussed previously, and a recovery from the City of Houston for right-of-way acquisition costs.

*Interlocal Agreement with METRO*

An agreement was reached with METRO whereby the cost of widening and reconstructing Hidalgo St. at an estimated cost of $1,184,569 was to be shared between METRO and the City. METRO provided $870,132.

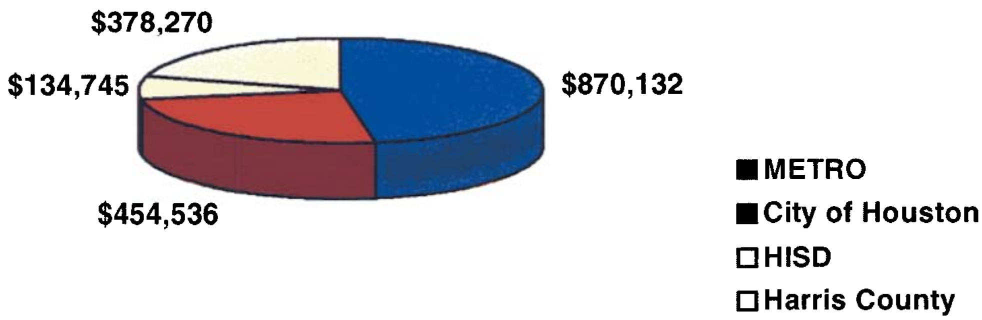
*Reimbursement for Right-of -Way Acquisition Costs*

On December 2, 1996, Ordinance 96-1336 approved the City's reimbursement to the Zone in the amount of $345,265 for right of way acquisition and associated costs incurred for street widening construction/reconstruction during 1993 that benefited the flow of traffic for the City rather than the Zone's residents.

*Funding by Taxing Unit and Taxpayer*

The chart below depicts funding received from other governments through of June 30, 1999.

**Intergovernmental Funding**




*Taxpayer Assessments*

In addition to property tax revenues two assessments have been levied to date — a capital assessment levied on the residents of PID #1 and an operational assessment levied on the residents of PID #2 — (PID #2 overlays PID #1 resulting in two assessments for PID #1 residents). The capital assessment was used to partially fund the project plan improvements within the boundaries of PID #1, therefore directly benefiting those residents.

The original capital assessment role was levied at a total of $1,567,729. Of which 51% was attributed to the principal landowner/developer. The average assessment for all other property owners totaled approximately $7,430.

The operational assessment is an annual assessment. The average assessment per parcel for the last two years approximated $550.

## Planned Revenues

Much of the Zone's financing plans were contingent on revenue plans based on future developments that were expected to take place quite rapidly after construction of the infrastructure improvements had taken place. Differences among the Developer and contractors, A downturn in the local economy and slow marketing efforts resulted in significant delays as development plans were stymied for at least two years. The table below illustrates the original estimated and actual captured appraised values by taxing unit and year:

**Planned Vs. Reported Taxable Appraised Values**

| Tax Year | Projected CAV | CAV - City of Houston | CAV - Harris County (3) | CAV - HISD (3) | Cumulative CAV |
|---|---|---|---|---|---|
| 1992 | | 14,390 | | | 14,390 |
| 1993 | | 2,668,220 | | | 2,668,220 |
| 1994 | 6,169,040 | 2,799,610 | 638,358 | | 3,437,968 |
| 1995 (1) | 16,435,820 | 10,086,300 | 7,156,808 | | 17,243,108 |
| 1996 | 24,244,820 | 11,413,550 | 8,068,898 | 10,170,103 | 29,652,551 |
| 1997 (2) | 32,224,820 | 12,123,600 | 8,797,248 | 10,625,863 | 31,546,71 |
| 1998 (4) | 39,972,820 | 18,761,020 | 15,011,578 | 19,228,143 | 53,000,741 |
| 1999 | 47,616,820 | | (fiscal year 2000) | | |
| 2000 | 51,074,820 | | (fiscal year 2001) | | |

*Notes*

(1) Infrastructure construction occurred
(2) Housing development occurred
(3) CAV is based on adjusted taxable values
(4) Tax Rates per $100 valuation are $.665 City, $ .416 County, $ .96 HISD

As shown above, captured appraised values have not met plan through June 30, 1999. However, total CAV began to meet projections in 1997 with the inclusion of Harris County's and HISD's participation.

The CAV shortfall directly impacted the Zone's tax increment revenues although the advance of tax increment funds by the City mitigated the cash flow impact. Delayed development also impacted utility revenues and assessment income as the projections for these revenue streams also assumed that development would begin reasonably soon and that property values would rise accordingly. In addition, as previously noted in the assessment section, many of the planned financing sources were delayed. Although actual revenues may indeed exceed projections in the future, delays have had a detrimental cash flow impact on the Zone historically.

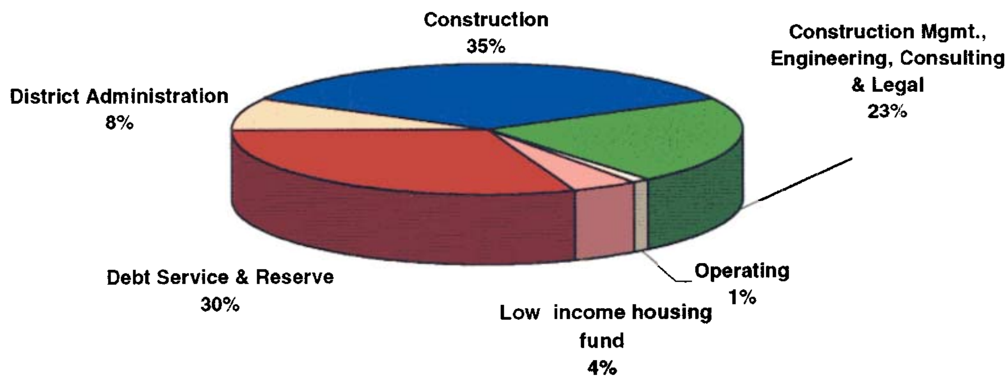
*Projections vs. Reported Assessments*

The Official Statement projected cash flows of approximately $1,337,124. While assessment income has exceeded projections by approximately $63,000, through June 30, 1999, the balance related to this assessment remaining uncollected was approximately $180,000 at June 30, 1999. Thus, actual cash flows were $120,000 less than projected.

# Uses of Funds — Planned Versus Reported

## Expenditures by Type

The chart below provides a brief overview of expenditures by type.




A more thorough analysis of expenditures is provided in a comparison of planned/budgeted expenditures provided below.

***Low Income Housing Fund***

As shown in the graph above $289,000 in expenditures went to providing low-income housing. While that amount may not be relatively significant to this point, it provides an economic benefit of the Zone that is not often considered. In addition, as the Zone continues to develop, this additional economic benefit generated by the Zone will certainly continue to grow in significance.

## Planned Versus Reported Expenditures

The following compares preliminary project estimates and Official Statement amounts to reported expenditures rather than a comparison of adopted budget to actual. However, it is important to note that these amounts were obtained from the planning documents which served as the key instrument in obtaining the necessary approvals and buy-in from impacted parties prior to the signing of formal agreements. In addition, performing such an analysis explains subsequent events and allows for improved future planning.

The analysis of planned versus reported expenditures is documented below in two distinct phases. The first phase is the Zone formation and construction period beginning immediately after the creation of the Zone and ending for analytical purposes on June 30, 1995; the fiscal year end, which captured all construction, related activity. The second period begins July 1995 and ends June 30, 1999. During this time period much of the redevelopment activity in the Zone was left to private developers and the Zone's principal operations consisted of planning, coordinating, and servicing the debt.

***Expenditures information through June 30, 1995***

The uses of funds, as proposed in the Official Statement contained the most recent estimates during this time period. A summary comparison is provided, as a detailed breakdown of the planned uses of funds per the Official Statement is not available.

| **Uses of Funds, Official Statement compared to Reported Expenditures** | Official Statement | Reported Expenditures through June 30, 1995 | Variance |
|---|---|---|---|
| Construction fund | $ 3,429,495 | $ 3,477,129 | $ (47,634) |
| Debt issuance, service and reserve funds | 983,424 | 555,595 | 427,829 |
| Organization and operation | 338,062 | 249,960 | 88,102 |
| | | | |
| Less - Debt reserve and issuance costs | 425,000 | – | (425,000) |
| | $ 4,325,981 | $ 4,282,684 | $ [illegible] |

Taking into account that approximately $425,000 in reserve and issuance costs should be removed for proper comparison with reported expenditures, then the Official Statement total becomes $4,325,981, which is comparable in total to reported expenditures.

All hard construction costs were performed under one major contract. Reported expenditures for this contract did not exceed original appropriated amounts.

Ordinance 92-1234 dated September 16, 1992, approved the Project Plan and the Finance Plan for the Zone. The Preliminary Project Plan Budget for Phases 1 & 2 was separated into Zone and PID #1 shares of the project plan. However, the Project Plan did not include administrative and debt service expenditures since they are not capital costs. Below is a comparative analysis of the Preliminary Project Plan dated September 16, 1992 compared to reported expenditures through June 30, 1995.

| | Preliminary Project Plan | Reported Expenditures Through June 30, 1995 | Variance (over)/under |
|---|---|---|---|
| **Capital Costs:** | | | |
| Water main items | $ 289,019 | 297,303 | (8,284) |
| Sanitary sewer items | 229,581 | 308,170 | (78,589) |
| Storm sewer/drainage items | 173,473 | 294,554 | (121,081) |
| Paving Items | 534,246 | 900,409 | (366,163) |
| Landscaping | 230,411 | 17,549 | 212,862 |
| Other work items | 267,936 | 125,395 | 142,541 |
| Street Lighting Items | 64,189 | 49,295 | 14,894 |
| Fencing | 110,911 | - | 110,911 |
| ROW Acquisition | - | 339,970 | (339,970) (1) |
| Contingencies | 189,977 | - | 189,977 |
| Engineering, architectural, legal, etc | 417,948 | 1,144,484 | (726,536) |
| Total | $ 2,507,691 | 3,477,129 | (969,438) |
| **Other:** | | | |
| Security & Sweeping Services | | $ 14,214 | |
| District Administration | | 235,746 | |
| Debt Service | | 555 595 | |
| Total Expenditures | | $ 4,282,684 | |

(1) This cost was later reimbursed.

*Construction Fund Variances*

As illustrated above in the Project Plan versus Reported Expenditures the following is noted:

- Water & Sewer infrastructure exceeded planned amounts by approximately $210,000.
- Paving items exceeded planned amounts by approximately $365,000.
- Right-of Way Acquisition amounted to approximately $340,000 that was not in the plan. These amounts were reimbursed in 1997 by the City of Houston and such funds provided for the subsequent completion of planned landscaping and fencing.
- Although it appears that engineering, architecture, planning and legal expenses exceeded plan by a significant amount; approximately $570,000 had been incurred by the Developer for architectural, urban planning, engineering and legal costs prior to construction. The costs were then paid by the City of Houston with bond proceed funds under the Reimbursement Agreement.

## Expenditures June 30, 1995 through June 30, 1999

As shown below, expenditures to date have consisted almost entirely of planning, administrative and debt service as there were no approved construction projects in place. As of June 30, 1999, combined unreserved fund balances amounted to approximately $1.4 million dollars before audit adjustments and restricted assets of approximately $300,000.

| | |
|---|---|
| Debt service | $ 1,094,398 |
| Engineering, architectural legal, etc. | 368,251 |
| District administration | 321,509 |
| Security & sweeping services | 45,395 |
| Other miscellaneous | 12,982 |
| | $ 1,842,535 |

### Events Subsequent to June 30, 1999

The Zone entered into an agreement in September 1999, with a Developer to reimburse approximately $2 million in development costs. As of March 31, 2000, the City has funded approximately $1 million on behalf of the Zone under this agreement.

# Control Enhancement Opportunities

Although management of the Zone rests with the Board of Directors, the Zone is reliant on several entities for a number of functions as follows:

- Day-to day operations are managed by the Zone Administrator, David Hawes, of Hawes, Hill, & Patterson, Consultants in consultation with the Department of Planning & Development of the City of Houston.

- Oversight and Final Authorization must be obtained from City Council for all assessments and project plans.

- The Office of the City Controller for the City of Houston performs accounting functions on behalf of the Zone.

- Collection and Liaison for Tax Increment Payments and PID #2 assessment are performed by the Collection Services – Tax Administration, Finance & Administration Department (F&A), City of Houston in conjunction with Harris County.

- Billing and collection responsibilities for PID #1 assessments rest with the Commercial Permitting and Enforcement Division of F&A.

  Tax Increment Calculations and Payments are performed by the individual taxing units which participate in the Reinvestment Zone - Harris County Tax Assessor Collector, HISD Tax Office, F&A, and the Harris County Appraisal District.

- The Public Works & Engineering Department administers the billing and collection of utility revenues.

- Construction management rests with the Public Works & Engineering Department.

- Investment and cash management controls are subject to the City's control processes, which also includes the calculation of interest earnings and processing of disbursements.

Given the number of parties involved and the plans to issue new bonds to continue redevelopment of the Zone, we commend City Controller, Sylvia Garcia and the Zone Administrator in championing this comprehensive audit to fully document all existing agreements and document the historical sources and uses of Zone funds. This effort provides the basis for improved communication and reporting in the future.

During this internal audit which covered eight fiscal years and multiple changes in management and accounting personnel, we identified opportunities to enhance the Zone's financial reporting to help ensure:

Stale balances are updated timely.

Fund balances are rolled forward.

Utility revenues are calculated and credited to the Zone.

Periodic analytical reviews are performed by Zone Management.

- We noted confusion among the taxing jurisdictions regarding the appropriate base year to utilize in performing tax increment calculations. We reviewed internal correspondence from the City's Legal Department related to base year calculations and recommend the City consider communicating the opinion of that legal review to the other taxing jurisdictions.

In summary, communication among the different parties charged with one or more Zone responsibilities should be improved to ensure there is a clear delineation and understanding of responsibilities. We recommend periodic meetings or communications be held to better coordinate efforts and action plans.

# Chronology of Events

## 1990

| | |
|---|---|
| November 7 | Creation of the Lamar Terrace Public Improvement District No. 1 (PID #1) |
| December 12 | Creation of the City of Houston, Texas, Reinvestment Zone No. 1 (the Zone) |

## 1991

| | |
|---|---|
| April 1991 | Residential Market Analysis performed by American Metro/Study Corporation |

## 1992

| | |
|---|---|
| March 18 | A one-year and five-year (1992-1996) Service and Assessment Plan was adopted by the City |
| May 6 | Reimbursement Agreement with Principal Landowner/Developer for the Establishment of the, Zone and PID #1 |
| September 16 | Approval of the first Project Plan and the Finance Plan for the Zone |
| October 7 | Planning and Zoning Regulations Passed for the Zone |
| November 24 | Bond Official Statement for TIF and PID Bonds issued |
| December | Inter-local Agreement with METRO |
| December 9 | Levy of Special Assessments for PID 1 |
| December 9 | Approval of Service Allocation Agreement |

## 1993

| | |
|---|---|
| January 1 | Enlargement of the Zone to incorporate the Westside |
| January 12 | Harris County Agreed to Participate in the Zone at 50% |

## 1995

| | |
|---|---|
| February 7 | Harris County Increased Participation to 100% |
| August 9 | Creation of the Lamar Terrace Public Improvement District #2 (District #2 is overlays PID 1, as the boundaries of PID 1 could not be enlarged) |

## 1996

| | |
|---|---|
| December 2 | Reimbursement to the Zone and PID 1 for Acquisition Costs of Land from the City |

## 1997

| | |
|---|---|
| January 29 | Approval of Inter-local Agreement with HISD |
| May 21 | Approval of Amended Reinvestment Zone Financing Plan |

## 1999

| | |
|---|---|
| May 11 | Amended Reinvestment Zone Project Plan and Financing Plan |
| June 9 | Agreement Between the Reinvestment Zone No. 1 and the Saint George Redevelopment Authority |
| August 10 | Third Amended Project Plan |

# Financial Schedules

Funding Sources

Tax Increment Calculation – City of Houston

Tax Increment Calculation – Harris County

Tax Increment Calculation – HISD

Use of Funds by Type

Expenditures by Year

Vendors Receiving Payments In Excess of $50,000

# Lamar Terrace
# Funding Sources
# Inception (November 7, 1990) through June 30, 1999

| Fiscal Year | Bond Proceeds | Inter - government | Tax Increments | Utility Revenues | PID Assessments | Miscella- neous Revenues | Interest | Total |
|---|---|---|---|---|---|---|---|---|
| **TIRZ #1** | | | | | | | | |
| 1999 | $ - | $ - | $ 224,393 | $ - | $ - | $ - | $ 27,624 | $ 252,017 |
| 1998 | - | - | 237,441 | - | - | - | 33,016 | 270,457 |
| 1997 | | 97,483 | 126,043 | 12,745 | - | - | 18,208 | 254,479 |
| 1996 | - | - | 94,913 | 14,184 | - | - | 19,939 | 129,036 |
| 1995 | - | - | 26,024 | 3,769 | - | 112 | 24,265 | 54,170 |
| 1994 | 86,599 | - | 21,095 | 11,497 | - | | 54,646 | 173,837 |
| 1993 | 2,095,844 | - | - | 5,288 | - | | 34,882 | 2,136,014 |
| Bond Gross up | 97,557 | - | - | - | - | - | - | 97,557 |
| | $ 2,280,000 | $ 97,483 | $ 729,908 | $ 47,484 | $ - | $ 112 | $ 212,580 | $ 3,367,567 |
| **PID #1** | | | | | | | | |
| 1999 | $ - | $ - | $ - | $ - | $ 82,945 | $ 857 | $ 17,495 | $ 101,297 |
| 1998 | - | - | - | - | 92,458 | 224 | 21,415 | 114,097 |
| 1997 | - | 279,932 | - | - | 104,548 | 9 | 20,363 | 404,852 |
| 1996 | - | - | - | - | 108,330 | 575 | 28,694 | 137,599 |
| 1995 | - | - | - | - | 122,607 | 755 | 24,200 | 147,562 |
| 1994 | 47,375 | - | - | - | 113,097 | 159 | 49,857 | 210,488 |
| 1993 | 718,332 | 870,132 | - | - | 773,482 | - | 33,876 | 2,395,822 |
| Bond Gross up | 34,293 | - | - | - | - | - | - | 34,293 |
| | $ 800,000 | $ 1,150,064 | $ - | $ - | $ 1,397,467 | $ 2,579 | $ 195,900 | $ 3,546,010 |
| **PID #2** | | | | | | | | |
| 1999 | $ - | $ - | $ - | $ - | $ 269,271 | $ 16,250 | $ 18,923 | $ 304,444 |
| 1998 | - | - | - | - | 265,394 | 1,425 | 12,128 | 278,947 |
| 1997 | - | - | - | - | 184,659 | 3,030 | 4,016 | 191,705 |
| | - | - | - | - | 719,324 | 20,705 | 35,067 | 775,096 |
| **Totals** | $ 3,080,000 | $ 1,247,547 | $ 729,908 | $ 47,484 | $ 2,116,791 | $ 23,396 | $ 443,547 | $ 7,688,673 |

## Lamar Terrace
## Tax Increment Calculation – City of Houston

**East Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1992 | $ 0.630 | $ 8,154,050.00 | $ 8,168,440.00 | $ 14,390.00 | 100% | $ 91 | $ 91 |
| 1993 | 0.630 | 8,154,050 | 10,822,270 | 2,668,220 | 100% | 16,741 | 16,810 |
| 1994 | 0.665 | 8,154,050 | 10,710,610 | 2,556,560 | 100% | 16,923 | 17,001 |
| 1995 | 0.665 | 8,154,050 | 14,765,560 | 6,611,510 | 113% | 49,723 | 43,967 |
| 1996 | 0.665 | 8,154,050 | 19,195,330 | 11,041,280 | 99% | 72,883 | 73,425 |
| 1997 | 0.665 | 8,154,050 | 20,125,940 | 11,971,890 | 91% | 72,194 | 79,613 |
| 1998 | 0.665 | 8,154,050 | 23,751,220 | 15,597,170 | 88% | 91,145 | 103,721 |
| | | | | | | $ 319,699 | $ 334,627 |

**West Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1994 | $ 0.665 | $ 18,573,540 | $ 18,816,590 | $ 243,050 | 100% | $ 1,612 | $ 1,616 |
| 1995 | 0.665 | 18,573,540 | 22,048,330 | 3,474,790 | 100% | 23,013 | 23,107 |
| 1996 | 0.665 | 18,573,540 | 18,945,810 | 372,270 | 98% | 2,434 | 2,476 |
| 1997 | 0.665 | 18,573,540 | 18,725,250 | 151,710 | 99% | 998 | 1,009 |
| 1998 | 0.665 | 18,573,540 | 21,737,390 | 3,163,850 | 96% | 20,104 | 21,040 |
| | | | | | | $ 48,160 | $ 49,248 |

**East & West Sides Combined**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1992 | | $ 8,154,050 | $ 8,168,440 | $ 14,390 | 100% | $ 91 | $ 91 |
| 1993 | | 8,154,050 | 10,822,270 | 2,668,220 | 100% | 16,741 | 16,810 |
| 1994 | | 26,727,590 | 29,527,200 | 2,799,610 | 100% | 18,535 | 18,617 |
| 1995 | | 26,727,590 | 36,813,890 | 10,086,300 | 105% | 72,736 | 67,074 |
| 1996 | | 26,727,590 | 38,141,140 | 11,413,550 | 99% | 75,317 | 75,900 |
| 1997 | | 26,727,590 | 38,851,190 | 12,123,600 | 95% | 73,192 | 80,622 |
| 1998 | | 26,727,590 | 45,488,610 | 18,761,020 | 92% | 111,249 | 124,761 |
| Accumulated Tax Increments through 1999 | | | | | | $ 367,860 | $ 383,875 |
| Accumulated Tax Increments through 1998 | | | | | | $ 256,611 | $ 259,114 |
| Accumulated Tax Increments through 1997 | | | | | | $ 183,419 | $ 178,492 |

# Lamar Terrace
# Tax Increment Calculation – Harris County

**East Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1994 | $ 0.3628 | $ 10,495,922 | $ 10,898,387 | $ 402,466 | 100% | $ 731 | $ 730 |
| 1995 | 0.4068 | 10,495,922 | 13,267,853 | 2,771,932 | 99% | 5,592 | 5,639 |
| 1996 | 0.4277 | 10,495,922 | 13,599,399 | 3,103,478 | 98% | 13,057 | 13,273 |
| 1997 | 0.4187 | 10,495,922 | 13,864,155 | 3,368,234 | 91% | 12,815 | 14,101 |
| 1998 | 0.4166 | 10,495,922 | 16,123,073 | 5,627,152 | 89% | 20,953 | 23,443 |
| | | | | | | $ 53,149 | $ 57,186 |

**West Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1994 | $ 0.3628 | $ 18,847,410 | $ 19,083,303 | $ 235,893 | 100% | $ 429 | $ 428 |
| 1995 | 0.4068 | 18,847,410 | 23,232,287 | 4,384,877 | 99% | 8,846 | 8,919 |
| 1996 | 0.4277 | 18,847,410 | 23,812,831 | 4,965,421 | 98% | 20,890 | 21,236 |
| 1997 | 0.4187 | 18,847,410 | 24,276,425 | 5,429,015 | 91% | 20,656 | 22,729 |
| 1998 | 0.4166 | 18,847,410 | 28,231,837 | 9,384,427 | 89% | 34,944 | 39,096 |
| | | | | | | $ 85,765 | $ 92,408 |

**East & West Sides Combined**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1994 | $ 0.3628 | $ 29,343,332 | $ 29,981,690 | $ 638,358 | 100% | $ 1,160 | $ 1,158 |
| 1995 | 0.4068 | 29,343,332 | 36,500,140 | 7,156,808 | 99% | 14,439 | 14,558 |
| 1996 | 0.4277 | 29,343,332 | 37,412,230 | 8,068,898 | 98% | 33,947 | 34,509 |
| 1997 | 0.4187 | 29,343,332 | 38,140,580 | 8,797,248 | 91% | 33,472 | 36,831 |
| 1998 | 0.4166 | 29,343,332 | 44,354,910 | 15,011,578 | 89% | 55,897 | 62,538 |
| Accumulated Tax Increments through 1999 | | | | | | $ 138,913 | $ 149,594 |
| Accumulated Tax Increments through 1998 | | | | | | $ 83,016 | $ 87,056 |
| Accumulated Tax Increments through 1997 | | | | | | $ 49,545 | $ 50,225 |

## Lamar Terrace
## Tax Increment Calculation – HISD

**East Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1996 | $ 0.96 | $ 8,186,800 | $ 16,829,610 | $ 8,642,810 | 99% | $ 82,233 | $ 82,971 |
| 1997 | 0.96 | 8,186,800 | 17,624,320 | 9,437,520 | 93% | 84,014 | 90,600 |
| 1998 | 0.96 | 8,186,800 | 23,276,070 | 15,089,270 | 90% | 131,067 | 144,857 |
| | | | | | | $ 297,313 | $ 318,428 |

**West Side**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1996 | $ 0.96 | $ 17,560,647 | $ 19,087,940 | $ 1,527,293 | 99% | $ 14,533 | $ 14,662 |
| 1997 | 0.96 | 17,560,647 | 18,748,990 | 1,188,343 | 99% | 11,301 | 11,408 |
| 1998 | 0.96 | 17,560,647 | 21,699,520 | 4,138,873 | 93% | 37,039 | 39,733 |
| | | | | | | $ 62,873 | $ 65,803 |

**East & West Sides Combined**

| Tax Year | Tax Rate per $100 val. | Base Year 1991 | Current Value | Current Increment | Collection Percent | Payable to Zone | Increment Revenues |
|---|---|---|---|---|---|---|---|
| 1996 | $ 0.96 | $ 25,747,447 | $ 35,917,550 | $ 10,170,103 | 99% | $ 96,766 | $ 97,633 |
| 1997 | 0.96 | 25,747,447 | 36,373,310 | 10,625,863 | 96% | 95,314 | 102,008 |
| 1998 | 0.96 | 25,747,447 | 44,975,590 | 19,228,143 | 92% | 168,106 | 184,590 |
| Accumulated Tax Increments through 1999 | | | | | | $ 360,186 | $ 384,231 |
| Accumulated Tax Increments through 1998 | | | | | | $ 192,080 | $ 199,641 |
| Accumulated Tax Increments through 1997 | | | | | | $ 96,766 | $ 97,633 |

## Lamar Terrace
## Use of Funds by Type

| | |
|---|---|
| Construction | $ 2,332,645 |
| Debt Service & Reserve | 2,090,033 |
| Construction management, engineering, consulting and legal | 1,512,735 |
| District Administration | 557,255 |
| Low income housing fund | 289,000 |
| Operating | 72,591 |
| Total expenditures by type | $ 6,854,259 |

# Lamar Terrace
# Expenditures by Year

| | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | Total |
|---|---|---|---|---|---|---|---|---|
| **TIRZ#1** | | | | | | | | |
| Expenditures | $ 660,504 | $ 930,681 | $ 17,851 | $ 306 | $ - | $ - | $ - | $ 1,609,342 |
| Debt Service | - | 179,154 | 176,700 | 176,700 | 177,006 | 176,700 | 176,700 | 1,062,960 |
| | 660,504 | 1,109,835 | 194,551 | 177,006 | 177,006 | 176,700 | 176,700 | 2,672,302 |
| **PID #1** | | | | | | | | |
| Expenditures | 257,695 | 1,933,378 | 2,049 | (30,458) | 303,400 | 64,584 | 50,842 | 2,581,490 |
| Debt Service | - | 56,778 | 106,000 | 102,500 | 99,402 | 95,500 | 92,000 | 552,180 |
| | 257,695 | 1,990,156 | 108,049 | 72,042 | 402,802 | 160,084 | 142,842 | 3,133,670 |
| **PID #2** | | | | | | | | |
| Expenditures | | | | | 54,524 | 118,107 | 148,878 | 321,509 |
| Debt Service | | | | | - | - | - | - |
| | - | - | - | - | 54,524 | 118,107 | 148,878 | 321,509 |
| Total expenditures | $ 918,199 | $ 3,099,991 | $ 302,600 | $ 249,048 | $ 634,332 | $ 454,891 | $ 468,420 | $ 6,127,481 |
| Low-income housing fund | | | | | | | | 289,000 |
| Debt service reserve and issuance costs | | | | | | | | 437,778 |
| Total uses of funds | | | | | | | | $ 6,854,259 |

## Lamar Terrace
## Vendors Receiving Payments in Excess of $50,000

| | | Total Payments |
|---|---|---|
| Hubco | $ | 2,008,359 |
| Robert Silvers | | 1,103,721 |
| Bank of New York Trust Co | | 982,701 |
| Nationsbank | | 398,002 |
| Terra Associates | | 239,450 |
| JTB Services | | 153,126 |
| Patricia Knudson & Associates | | 142,168 |
| HH&W Consultants | | 107,273 |
| David Hawes Consulting | | 81,241 |
| Vinson & Elkins | | 55,605 |
| Hawes, Hill & Patterson | | 53,703 |
| | $ | 5,325,349 |