

City of Houston, Texas

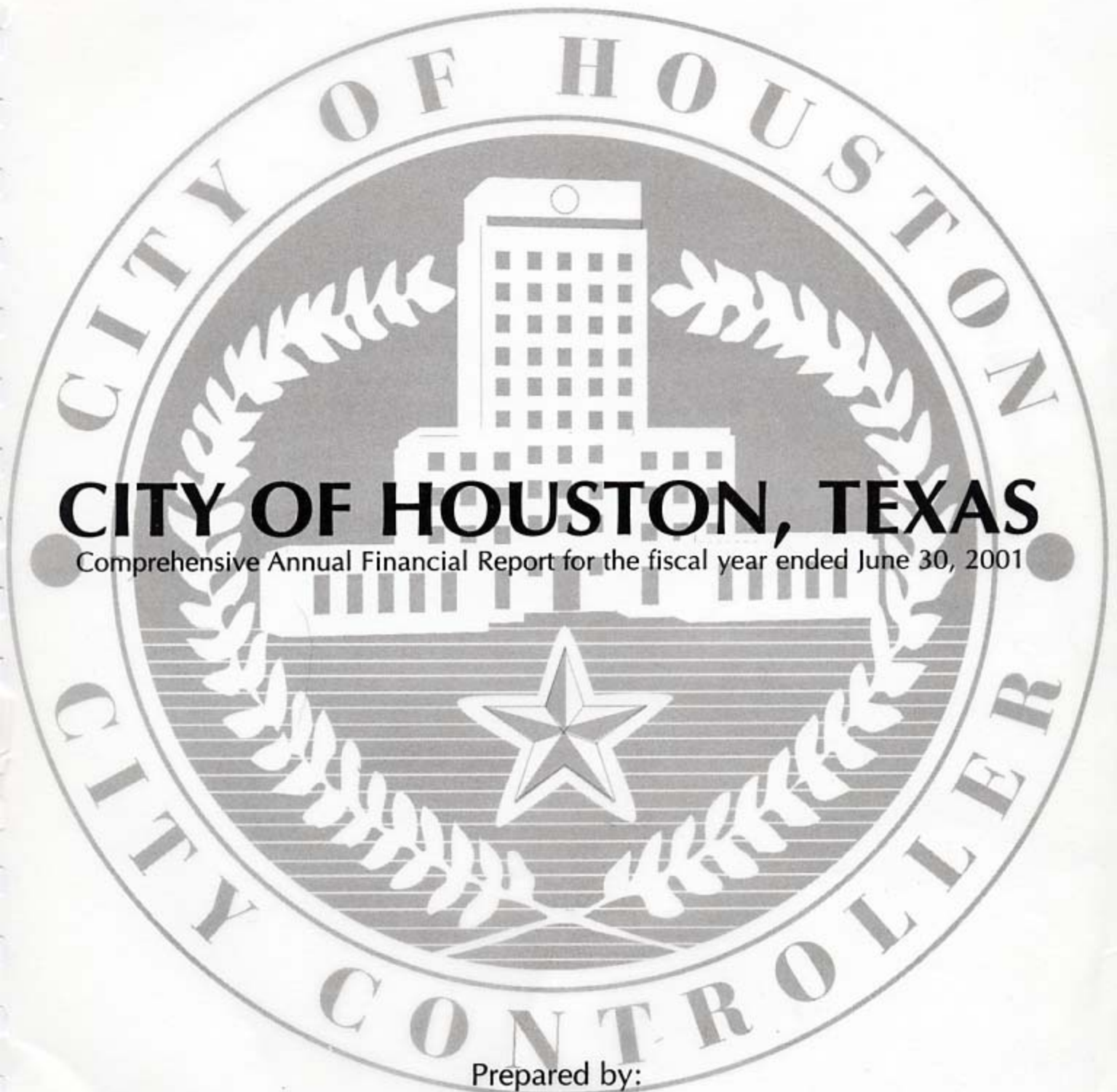


**Comprehensive Annual Financial Report
for the fiscal year ended June 30, 2001**

Sylvia R. Garcia
City Controller



OFFICE OF THE CITY CONTROLLER 98 YEARS OF HOUSTON HISTORY



CITY OF HOUSTON, TEXAS

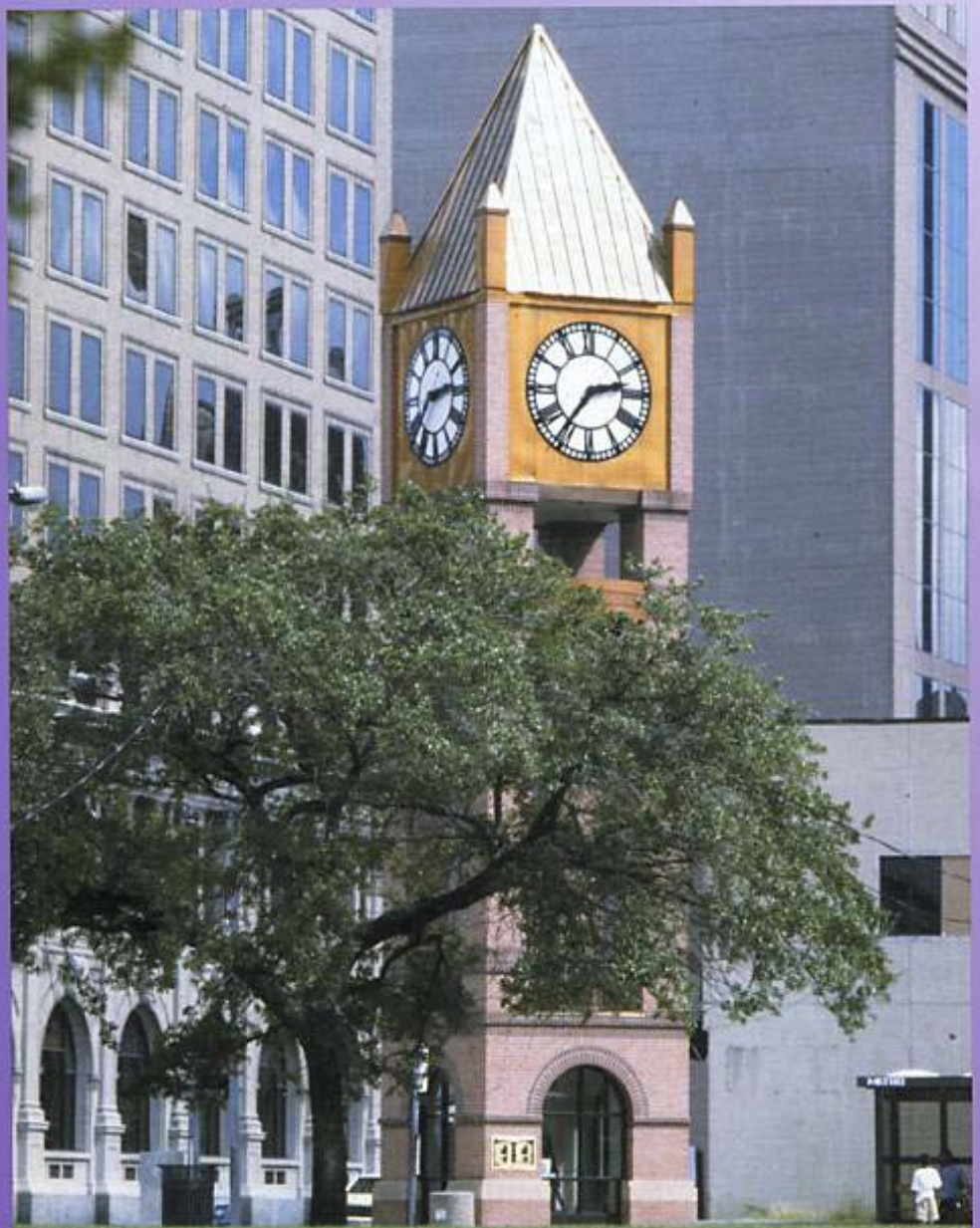
Comprehensive Annual Financial Report for the fiscal year ended June 30, 2001

Prepared by:

Sylvia R. Garcia, JD, City Controller

Judy Gray Johnson, CPA, Chief Deputy City Controller

Larry Homan, CPA, Director, Financial Reporting Division



Time and Time Again

Located in downtown Houston next to Market Square, the restoration of this clock tower helps to preserve Houston's history. Once part of Houston's commercial district, Market Square now features restaurants and entertainment venues in historic buildings and offers public art in a park-like setting.

**CITY OF HOUSTON, TEXAS
 COMPREHENSIVE ANNUAL FINANCIAL REPORT
 For the Year Ended June 30, 2001**

	Page
Introductory Section	
Office of the City Controller	i
City Controller	ii
Organizational Chart for the Office of the Controller	iii
Mayor, City Controller and City Council Members /Elected Officials	iv
Organizational Chart for Houston City Government	v
Transmittal Letter	vii
Certificate of Achievement for Excellence in Financial Reporting	xxvi
Financial Section	
Independent Auditor's Report	
	1
General Purpose Financial Statements:	
Combined Balance Sheet - All Fund Types, Account Groups and Discretely Presented Component Units	4
Combined Statement of Revenues, Expenditures and Changes in Fund Balances - All Governmental Fund Types, Expendable Trust Funds and Discretely Presented Component Units	8
Combined Statement of Revenues, Expenditures and Changes in Fund Balances - Budget and Actual - General, Special Revenue, and Debt Service Funds	10
Combined Statement of Revenues, Expenses and Changes in Fund Equity - All Proprietary Fund Types	12
Combined Statement of Changes in Plan Net Assets - Pension Trust Funds	13
Combined Statement of Cash Flows - All Proprietary Fund Types	14
Combining Balance Sheet - Discretely Presented Component Units	16
Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Discretely Presented Component Units	20
Notes to the General Purpose Financial Statements	25
Required Pension System Supplementary Information	58
Combining Individual Fund and Account Group Financial Statements and Schedules	
General Fund	
Balance Sheets	62
Statements of Revenues, Expenditures and Changes in Fund Balances	63
Schedule of Budgeted and Actual Revenues	64
Schedule of Budgeted and Actual Expenditures	65
Special Revenue Funds	
Combining Balance Sheet	70
Combining Statement of Revenues, Expenditures and Changes in Fund Balances	74
Statement of Revenues, Expenditures and Changes in Fund Balances - Budget and Actual	
Asset Forfeiture Fund	78
Auto Dealers Fund	79
Building Inspection Fund	80
Cable Television Fund	81
Fire Prevention Fund	82
Houston Transtar Fund	83
Parks Special Fund	84
Police Special Services Fund	85
Sign Abatement Fund	86
Sign Administration Fund	87
Street and Drainage Maintenance Fund	88
Street Maintenance and Traffic Control Fund	89
911 Emergency Network Fund	90
Signal Maintenance Fund	91

CITY OF HOUSTON, TEXAS
COMPREHENSIVE ANNUAL FINANCIAL REPORT
For the Year Ended June 30, 2001

	Page
Debt Service Fund	
Balance Sheets	94
Statement of Revenues, Expenditures and Changes in Fund Balances	95
Capital Projects Fund	
Balance Sheets	98
Statements of Revenues, Expenditures and Changes in Fund Balances	99
Enterprise Funds	
Combining Balance Sheet	102
Combining Statement of Revenues, Expenses and Changes in Fund Equity	106
Combining Statement of Cash Flows	108
Airport System	112
Convention and Entertainment Facilities Fund	116
Water and Sewer System	120
Sports Arena	124
Internal Service Funds	
Combining Balance Sheet	128
Combining Statement of Revenues, Expenses and Changes in Fund Equity	129
Combining Statement of Cash Flows	130
Fiduciary Funds	
Combining Balance Sheet	132
Expendable Trust Funds	
Combining Balance Sheet	134
Combining Statement of Revenues, Expenditures and Changes in Fund Balances	138
Pension Trust Funds	
Combining Statement of Plan Net Assets	142
Combining Statement of Changes in Plan Net Assets	144
Agency Funds	
Combining Statement of Changes in Assets and Liabilities	146
General Fixed Assets Account Group	
Schedule of General Fixed Assets by Source	150
Schedule of General Fixed Assets by Function and Activity	151
Schedule of Changes in General Fixed Assets by Function and Activity	152
General Long-Term Debt Account Group	
Comparative Schedules of General Long-Term Debt	156
Statistical Section (unaudited)	
General Revenues by Source	158
General Expenditures by Function	160
Airport System Fund Revenues and Expenses	164
Convention and Entertainment Facilities Fund Revenues and Expenses	166
Water and Sewer System Fund Revenues and Expenses	168
Property Tax Levies and Collections	170
Taxable Values and Tax Levies	172
Property Tax Rates - All Direct and Overlapping Governments	174
Ratio of General Bonded Debt to Taxable Value and Bonded Debt per Capita	176
Ad Valorem Tax Obligation Percentages by Tax Year	178
Computation of Legal Debt Margin	179

CITY OF HOUSTON, TEXAS
COMPREHENSIVE ANNUAL FINANCIAL REPORT
For the Year Ended June 30, 2001

	Page
Statistical Section (unaudited)	
Computation of Direct and Overlapping Debt	180
Ratio of Annual Debt Service Expenditures for General Bonded Debt to Total General Governmental Expenditures	181
Outstanding Principal Amount of Obligations Payable From Ad Valorem Taxes and Other Revenue Sources	182
Principal Taxpayers/Mixed Beverage Taxes	183
Employment Statistics	184
Construction and Bank Deposits	186
Revenue Bond Coverage	187
General Fund Budget for Fiscal Year 2002	188
Tax Supported Debt Service Funds - Tax Bond and Certificates Debt Service Fund for Fiscal Year 2002	189
Continuing Debt Disclosure Information	190
Convention and Entertainment Facilities Statistics	192
Water and Sewer System Statistics	198
Water and Sewer System Statistics - Debt Service Schedule	203
Water and Sewer System Statistics - Water Supply	204
Airport System Statistics - Passenger Statistics	206
Airport System Statistics - Airline Market Shares	208
Airport System Statistics - Selected Financial Information	210
Airport System Statistics - Total Aircraft Operations and Aircraft Landing Weight	212
Airport System Statistics - Summary of Certain Fees and Charges	213
Airport System Statistics - Debt Service Schedule	214
Airport System Statistics - Service Area	215
Demographic Statistics	216
Surety Bond and Insurance Coverage	221
Salaries of Elected Officials	223
Schedule of Credits	224



Office of the City Controller

Houston's City Controller, Sylvia R. Garcia, is the second highest elected official in Houston City government and its chief financial officer, as dictated by the City charter. The Office of the City Controller superintends the fiscal affairs of the City, which includes conducting audits, managing its investment and debt, preparing financial statements and providing leadership on issues pertaining to the City's financial health. She thus serves as an independently elected "financial voice" on issues of importance to the City.

Now ending her second term, Controller Garcia continues to build upon the improvements she established in the Office's audit services, customer services, financial reporting, investment management and technology. By promoting more efficient and effective governmental operations, the Office of the City Controller has identified tens of millions of dollars in potential savings to City government.

Technological upgrades bring office operations a step closer to "paperless" transactions. The pilot project that began in FY2000 is now used by most City departments. This allows direct review of records over the City's computer network. We no longer need to print hard copies of documents and send them through interoffice mail, and this does away with the need for departments to maintain duplicate filing systems. Once implemented across the entire City, it will significantly reduce time to process paperwork as well as the amount of paper used. We conducted the second Internet-based bond sale this year, refining the auction process, and achieving near-record low interest rates. Meanwhile, the "positive pay" check security system continues to capture phony and altered checks, saving the City, in some cases, hundreds of thousands of dollars.

Enhanced audit functions, including more audit personnel on staff, as well as the use of sophisticated computer software, enabled the Office of the City Controller to complete 42 audits in FY2001. The new software helps to manage the audit process and is used for extracting and analyzing financial data. This reinforces the risk-based audit approach by identifying exceptions that indicate an audit may be necessary.

Next year's Comprehensive Annual Financial Report will be the first to reflect the new reporting model required by the Governmental Accounting Standards Board in its Statement 34. The inclusion of new citywide financial statements on the full accrual basis including infrastructure assets and depreciation in addition to individual governmental fund statements presented on the modified accrual basis provides a major challenge for the Controller's Office.

In fiscal year 2001, the City Controller expanded the use of the office as an economic resource for City government and the city as a whole. The image of the Office of the City Controller as a credible, fiscally prudent operation continues to strengthen, and the view of the City Controller as the City's "financial voice" is now well established.

The preparation of the Comprehensive Annual Financial Report (CAFR) requires a concentrated effort by every division of the City Controller's office. The Financial Reporting Division is ultimately responsible for the final product. The CAFR will be available on the City Controller's website, found at www.cityofhouston.gov/electedofficials/citycontroller.html



SYLVIA R. GARCIA

HOUSTON CITY CONTROLLER



Houston City Controller Sylvia R. Garcia is a native of the South Texas farming community of Palito Blanco. She attended Texas Woman’s University on a scholarship, graduating with a degree in social work, and received her Doctor of Jurisprudence degree from Thurgood Marshall School of Law at Texas Southern University. The eighth of 10 children, she learned at an early age the value of education and hard work. She also learned to be frugal with a dollar; a lesson which serves her well in the Office of the Controller.

Controller Garcia was sworn in on January 2, 1998 as Controller for the City of Houston. She is the second-highest City elected official and serves as the City’s Chief Financial Officer. Prior to her election in November 1997, Controller Garcia served as the appointed Director and Presiding Judge of the Houston Municipal Court System. As Presiding Judge, she was responsible for a multi-million-dollar budget, coordinated a staff of 50 judges, and established the operation and administration policies of the courts. She enjoys the distinction of having served for an unprecedented five terms under two mayors. Controller Garcia believes that maintaining the City’s fiscal soundness is serious business and is committed to ensuring that City government operates cost-effectively.

Active in the Houston community, the Controller has served on more than 25 community boards and commissions, including the San Jacinto Girl Scouts, the Houston Hispanic Forum, the American Leadership Forum, the Texas Southern University Foundation and the Institute of Hispanic Culture.

Despite her duties as City Controller, Ms. Garcia has made the time and commitment to be the chairperson or honorary chairperson of numerous charity functions. These include the “1998 Girls Inc. Charity Gala” and the kick-off for “America Walks for Strong Women”.

Controller Garcia has been honored by community leaders and the media. In 2001 she was named “Texas Woman to Watch” by the Business and Professional Women of Texas. She has also been named “Humanitarian of the Year” by the National Conference of Communities and Justice and was chosen as one of “Houston’s 25 Power People” by Inside Houston magazine. The Houston Press also named her “Politician of the Year.”

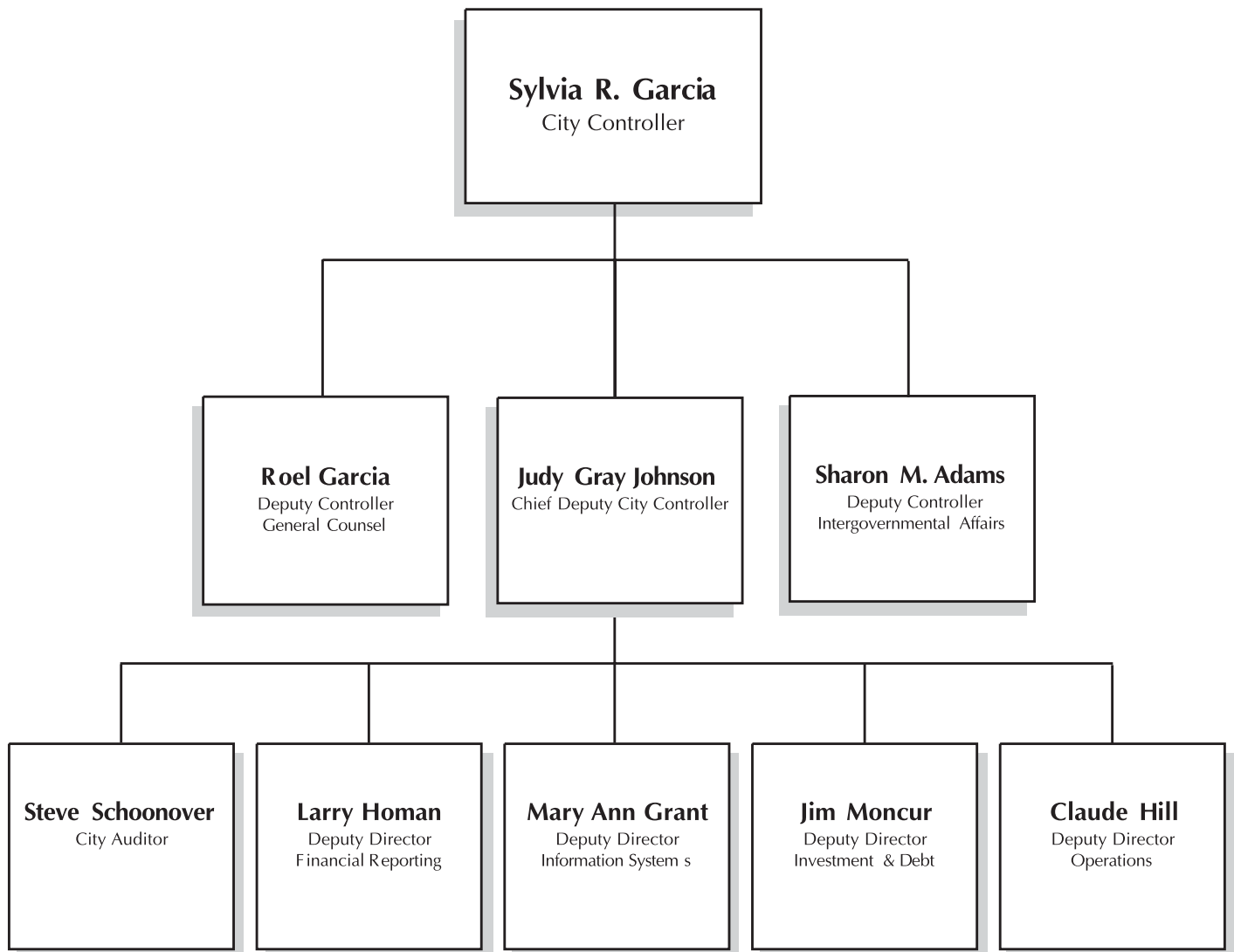
In 2001 Controller Garcia received the Distinguished Local Government Leadership Award from the national Association of Government Accountants (AGA). Other recent honors include the receipt of the Texas Woman’s University Board of Regents Woman of Distinction Award, the Hispanic Scouting Distinguished Citizen Award from the Sam Houston Area Council/Boy Scouts of America and the Board Award from the San Jacinto Girl Scouts.

Before joining the City, Controller Garcia worked as an attorney for the Gulf Coast Legal Foundation and served on the City’s first Appraisal Review Board. She also served as administrative law judge for the Equal Employment Opportunity Commission and headed her own law firm.



City of Houston

The Office of the City Controller





Elected Officials City of Houston, Texas



Mayor

Lee P. Brown

City Controller

Sylvia R. Garcia

Council Members

Jew Don Boney, Jr., **Mayor Pro-Tem, District D**

John E. Castillo, **Vice Mayor Pro-Tem, District I**

Annise Parker, **Position 1** Gordon Quan, **Position 2**

Orlando Sanchez, **Position 3** Chris Bell, **Position 4** Carroll G. Robinson, **Position 5**

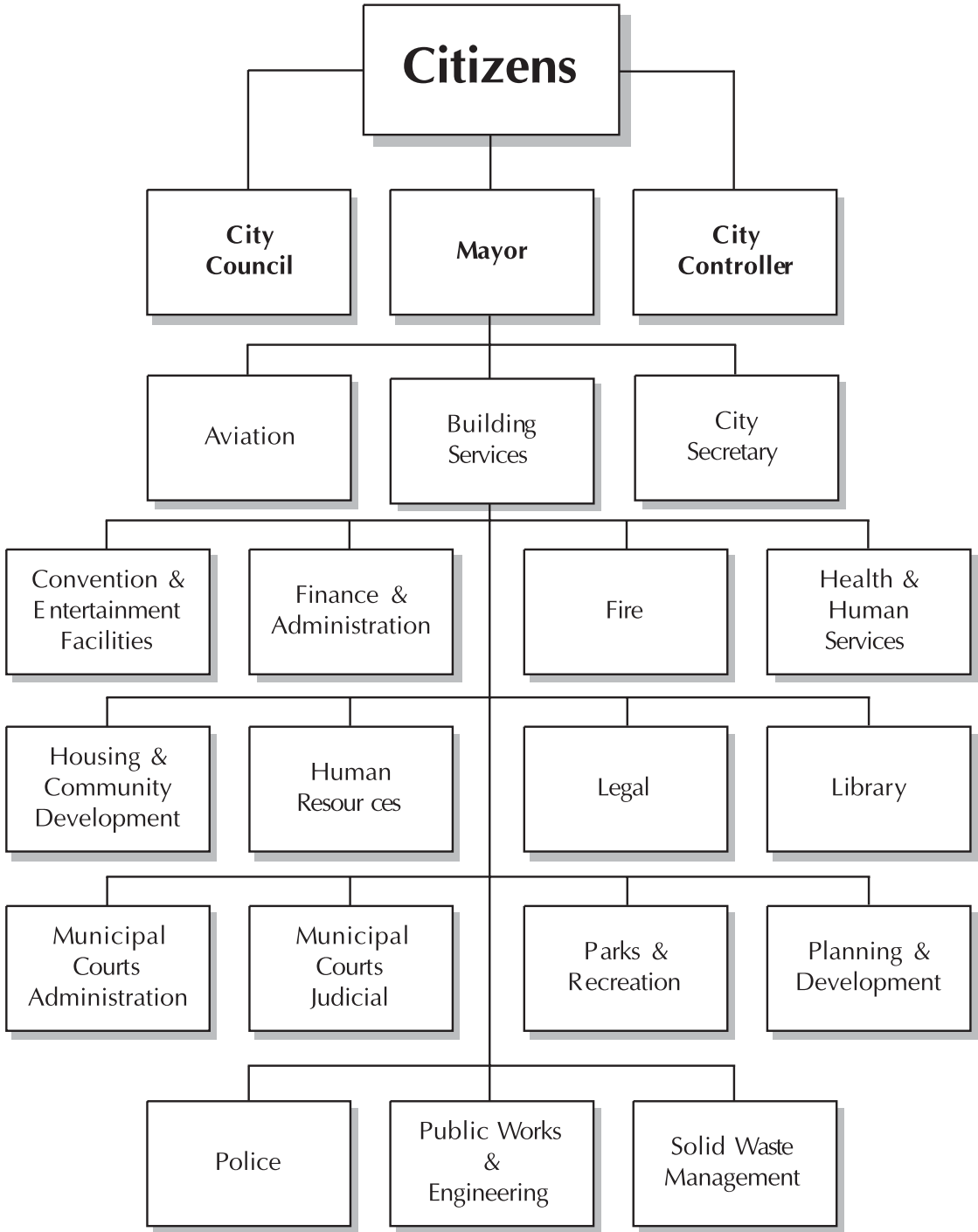
Bruce Tatro, **District A** Carol M. Galloway, **District B**

Mark Goldberg, **District C** Rob Todd, **District E**

Mark A. Ellis, **District F** Bert Keller, **District G** Gabriel Vasquez, **District H**

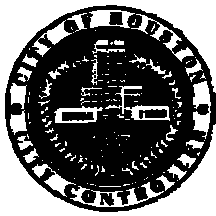


Organization Chart City Government



CITY OF HOUSTON, TEXAS





**OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS**

November 30, 2001

Honorable Mayor and City Council Members
Houston, Texas:

I am pleased to provide you with the Comprehensive Annual Financial Report (CAFR) of the City of Houston, Texas (City) for the year ended June 30, 2001, including the independent auditors' report. The CAFR was prepared by the City Controller's Office and satisfies my responsibilities under state law. The accuracy of the financial statements together with the completeness and fairness of their presentation are the responsibility of the City's management. The enclosed data is accurate in all material respects and the report has been designed to present fairly the financial position and results of operations of the various fund and account groups of the City in accordance with generally accepted accounting principles (GAAP), as established by the Governmental Accounting Standards Board (GASB).

The CAFR is presented in three sections: introductory, financial, and statistical. The introductory section includes this transmittal letter, a list of principal City officials, the City's organizational charts for the Office of the City Controller and for Houston's city government, and a copy of the Government Financial Officers Association's Certificate of Achievement for Excellence in Financial Reporting for the City's 2000 CAFR. The financial section includes the general-purpose financial statements, the combining and individual fund financial statements and schedules, as well as the auditors' report on the general purpose financial statements. The statistical section includes selected financial and demographic information generally presented on a multi-year basis.

This Comprehensive Annual Financial Report reflects the financial status of the City of Houston as of June 30, 2001. Since that time, Houston has experienced the effects of a national recession as well as the aftershock of the events of September 11th. These factors, combined with a general downturn in certain sectors of the City's economy, may change the financial outlook for Houston.

The Reporting Entity and Its Services

This report includes all funds and account groups of the City as well as those legally separate organizations for which the City is financially accountable. The City's determination of "financial accountability" is in accordance with Statement No. 14 of the Governmental Accounting Standards Board, *The Financial Reporting Entity*.

The City provides a full range of municipal government services to over 1.9 million residents and to an estimated 21 million conventioners and other visitors annually. Municipal services provided include police and fire protection, emergency medical services, pretrial detention services, traffic and municipal courts, water production and distribution, solid waste collection and disposal, sanitary code enforcement, health and human services, building and housing code enforcement, construction and maintenance of streets and certain bridges, traffic signal installation and maintenance, parks and recreation, library, cultural and convention activities, and

operation of three municipal airports, including George Bush Intercontinental, William P. Hobby, and Ellington Field.

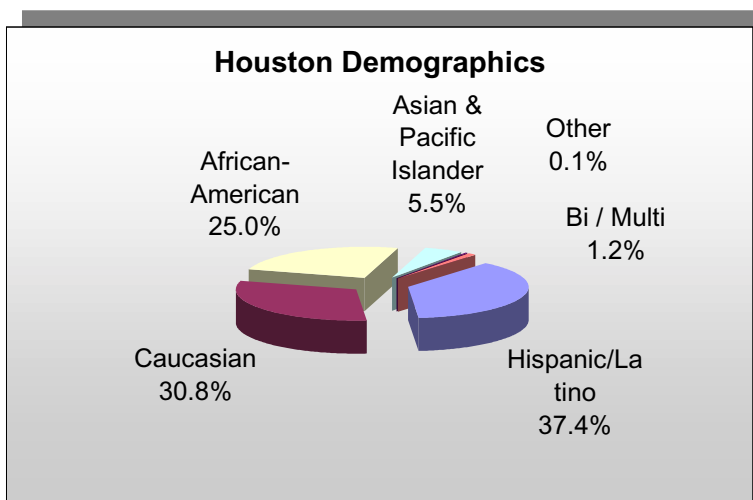
The City does not operate hospitals, schools, transportation systems, or higher education systems. Special districts and governmental entities with independent taxing authority administer the public hospitals and public schools within the City.

The Local Economy and Outlook

Houston leads the energy industry with more than one fourth of U.S. crude petroleum and gas extraction jobs located in the metro area, where 48 of the nation's 200 largest extraction/production companies are based. Also, 13 of the world's 20 largest natural gas transmission companies operate headquarters in Houston, and almost half the world's oil and gas field machinery is produced by companies contributing to Houston's economic success. Every major gas exploration and production company operates in Houston.

Houston is well known as the energy capital of the world, but has also attained world-class prominence in other industries due to its tremendous wealth of natural and human resources. A major corporate center, Houston ranks fifth among U.S. metropolitan areas in the number of corporate headquarters of Fortune 500 companies with 21. Cendant Mobility, the world's largest relocation company, recently named Houston the most popular city for relocating employees transferring within the United States. More than half the world's 100 largest non-U.S.-based corporations have operations in Houston. In addition to energy, leading industries include engineering and construction, real estate, aerospace and space commerce, medicine and health care, transportation, biotechnology, computer hardware and software technology, and electronics and telecommunications.

The fourth-largest city in the U.S. and the largest city in Texas, Houston's population exceeds 1.9 million. Seventy-four consular offices, forty foreign chambers of commerce and trade associations and twenty-five foreign-owned banks from eleven nations have helped make Houston both an international and a culturally diverse city. The 2000 Census indicates that the City of Houston is 37.4% Hispanic (includes all races), 30.8% Caucasian, 25.0% African-American, 5.5% Asian and .1% other and 1.2% bi- or multi-racial.



An exciting development in the Houston area involves the Quality of Life Coalition, which is a group of citizens from the civic, business and environmental communities who are working together to enhance life in Houston. The Coalition works in four main areas: trees and landscaping, parks and bayous, billboards and signage, and litter and graffiti. Houston boasts 17.6 acres of parks for every 1000 people, and the Coalition is working to increase this ratio. Also, Houston's Clean Neighborhood Program, part of Keep Houston Beautiful, is a nationally

acclaimed public-private partnership. All sectors of the community are working together to enhance the beauty of this major urban center, which in turn promotes continued prosperity. Tourism is a growing industry in Houston. During 1998-1999, 41 million people visited the Houston area, of which 62% were leisure travelers and over half visited a cultural or leisure attraction. Foreign travel has grown in Houston as well with over 5.6 million international passengers traveling through Bush Intercontinental Airport in 2000. Houston visitors spend an average of \$102 per day. In 1999, travel generated more than \$147 million in tax revenue for the Houston PMSA, while in 2000 hotel/motel room revenue was more than \$845 million. More than twenty-one million people visit Houston each year. Major attractions include the city's Theater District, the annual Houston Livestock Show and Rodeo, NASA Johnson Space Center and Space Center Houston, sports venues, museums, expansive hotel and convention facilities, and retail centers. Tourism makes up a vibrant portion of the city's revenues, generating a job payroll of over \$2.09 billion or approximately 89,100 jobs.

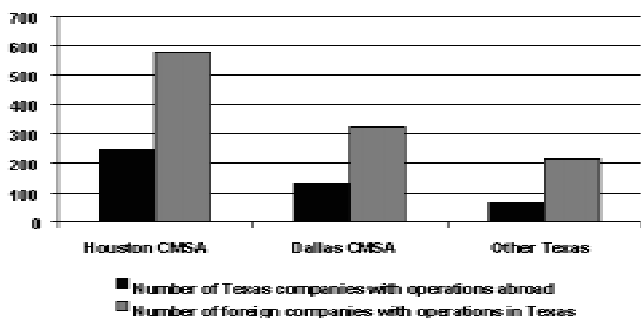
Houston has a highly skilled workforce and well-educated populace with almost 25% of adult Houstonians completing four or more years of college, compared with 20.3% nationally. In surveys conducted nationwide over the past decade, Houston has distinguished itself as a city with a positive attitude.

Economic Data

- Houston's economy was recently ranked seventh in the U.S. and 30th in the world.
- The population of Houston's Primary Metropolitan Statistical Area (PMSA) exceeded 4.6 million as of April 1, 2000 as compared to approximately 3.9 million at July 1, 1998.
- Houston has a very technology oriented workforce, with 60% more technology workers than expected for a city of its size.



Multinational Firms in Texas



Source: Texas Dept. of Economic Development, 1996

Over the past two decades the City has diversified its business base to become a leading international business center. In 1999, over 3,400 Houston companies reported having business activities abroad. Also, more than half of foreign companies with operations in Texas are located in Houston. The North American Free Trade

Agreement (NAFTA) enables Houston to gain prominence as a hub of foreign trade. More than half the world's 100 largest non-U.S.-based companies currently have operations in Houston. The growth of Johnson Space Center and the building of the international space station have made Houston a center for the aerospace industry as well.

Technology is also an important industry in Houston. The Houston Advanced Research Center, a renowned facility, focuses on scientific research and applied technology development. Some 150 companies benefit annually from the Center's research. The energy industry, centered in Houston, also invests heavily in technology and research and development, enhancing technological progress in Houston. In the future, Houston will benefit from the expansion of the bioscience, medical and healthcare industries, as well as the computer and electronics fields. Cutting edge research occurs in the Texas Medical Center, located in Houston, where the first artificial heart implant was completed by Dr. Michael DeBakey in 1966. The Texas Medical Center includes over 42 institutions today and covers 675 acres in Houston. It is where the first and still largest air emergency service was created, and more heart surgeries are performed there than anywhere in the world. The Medical Center also receives over \$350 million annually in funded research. If the Medical Center institutions were considered to be a single entity, it would be the largest employer in Houston with 49,000 employees and the largest medical center in the world with around 3.8 million patient visits annually.

Outlook

The economic outlook for Houston at this time is unclear. A review of current economic data reveals indicators in different directions. During the fiscal year ended June 30, 2001, while the employment growth rate nationally dropped from 2.5% to zero, the employment growth rate in the Houston area remained above 2%. The Greater Houston Partnership recently predicted that job growth in Houston will be only 0.7% in 2002. On the other hand, the Houston area's existing-home sales in October 2001, propped up by the low mortgage rates, were the highest ever for the month of October, up 2.3 percent from last year. A string of corporate mergers, layoffs and even bankruptcy, involving some of Houston's major corporations, such as Enron Corp., Compaq Computer Corp. and Continental Airlines, also threaten to injure the local economy. It is not possible to estimate the economic impact of the tragic events for September 11, 2001, or the subsequent war on terrorism.

Initiatives and Accomplishments

Houston is a culturally diverse international city, which is focused on the future and committed to enhancing the quality of life for its citizens. Major initiatives implemented by City leaders over the past year will ensure the continued success of Houston in the 21st century.

Mayor Lee P. Brown and City Controller Sylvia R. Garcia both took office in January 1998 as the City's top two elected officials.

Mayor Brown's initiatives and accomplishments are a reflection of the five guiding principles that are the foundation of his administration. These are as follows:

- Neighborhood Oriented Government
- Opportunities for Youth

- Transportation and Infrastructure
- Economic Development and International Trade
- Continuous Improvement

City Controller Garcia's initiatives and accomplishments are a reflection of the mission of the City Controller's Office, which is to superintend and supervise the fiscal affairs of the City of Houston and to manage and conduct the same as prescribed by the City Charter and the City Code of Ordinances. The City Controller's Office had several significant accomplishments during fiscal year 2001. Some of these accomplishments and initiatives are as follows:

- Implementation plans began during fiscal year 2001 in order to fulfill Governmental Accounting Standards Board Statement No. 34 Basic Financial Statements – and Management Discussion and Analysis – for State and Local Governments (GASB 34) requirements. GASB requires the City of Houston implementation for the fiscal year ending June 30, 2002, which began on July 1, 2001. This new reporting model introduces government-wide financial statements and will include for the first time a required management discussion and analysis (MD&A) that gives readers an objective and easily readable analysis of the government's financial performance for the year.
- The City Controller's Office has implemented a project to increase the imaging capabilities of the City's computer network. The project allows City department personnel to directly retrieve records over the network that otherwise would require the Controller's Office to produce a hardcopy and send it to the requestor. Most of the departments are now using the new system. Once implemented across the entire City, it could significantly reduce time to process paperwork as well as the amount of paper used.
- The Controller's Office web site has been expanded, with up to date information including copies of audit reports, quarterly investment reports, the Comprehensive Annual Financial Report, monthly financial reports and other useful information.
- In June, the City Controller's recommendation for a Rainy Day Fund was approved by Council effective FY2002. Our office has long advocated for the creation of such a fund to help the City prepare for unanticipated expenditures during slower economic times. The fund is an important component of the fiscally prudent course of action proposed by the Office of the City Controller since 1998.

Throughout the City

The tragedy of September 11 superseded all other national events in 2001, and the aftereffects will undoubtedly impact the City of Houston in as yet undetermined ways. Earlier in the year, however, Houston experienced its own tragedy when the most devastating tropical storm in the nations' history. Tropical Storm Allison struck the area in the early hours of the morning on June 9th. Over 60,000 homes and businesses were damaged, and 22 people lost their lives. The cleanup has been completed, as well as repairs to many of the buildings. FEMA has paid over \$500 million to flood victims in the area. The Houston area is on the road to recovery from this disaster.

In spite of recent flooding, exciting changes are occurring throughout the Houston area. Downtown Houston is alive with major revitalization efforts. Bayou Place, a 155,000 square-foot

retail and entertainment complex including a multi-plex cinema, a concert performance hall, trendy restaurants and other venues, is alive and thriving on evenings and weekends. Bayou Place Phase II, a 40,000+ square-foot expansion, has been completed and is now leasing. Construction is underway on the Hobby Center for the Performing Arts, the future home of Theater Under the Stars and the Humphreys School of Musical Theatre. Scheduled to open in 2002, the \$75 million facility will have two stages with seating capacity for 2,650 and 500 attendees, respectively.

Across the street in City Hall, the Greater Houston Convention and Visitors Bureau operates a visually appealing Visitor Center. It features area guides and brochures, video kiosks, a theater, and state of the art touch screen computers to guide visitors through accommodations, dining, and other attractions in the city and surrounding area.

Houston will greatly increase its capacity to host large conventions with the completion of the new Hilton convention center headquarters hotel and expanded George R. Brown Convention Center. Both the hotel, with 1,200 rooms and 70,000 square feet of meeting space including two ballrooms, and the convention center expansion are currently underway and designed with expected openings in 2003. The most exciting news, however, is the Instrumentation Systems and Automation Society's plan to hold its annual exposition, expected to draw 35,000 in international attendance, in the new convention center and hotel complex in 2006.

One of the most eagerly anticipated downtown undertakings is Cotswold 2000, a landscape, streetscape, and parking beautification project nearing completion that will add new streetlights and fountains through downtown Houston. The project is expected to dramatically improve the aesthetics and the pedestrian character over 90 city blocks, including Market Square. Cotswold 2000 planners anticipate that upon completion at the end of 2002, the project will become a focal point for entertainment and commerce, making downtown Houston a more beautiful place to live and work.

The City of Houston is embarking on another beautification project involving Buffalo Bayou. Traversing the city limits and downtown area, the Bayou will become a scenic link for the city. Beautification efforts include a master plan and study as well as landscaping and the placement of public art, decorative lighting, and park benches as well as other amenities.

Enron Field, the home of the Houston Astros baseball team, opened on March 30, 2000. The \$250 million stadium officially seats 40,950 and attracted over 3 million fans in the 2000 season and over 2.9 million fans in the 2001 season. Additionally, the new yet to be named Downtown Arena, future home of the Houston Rockets NBA basketball team and the Houston Comets WNBA women's team, is also to be built nearby the Brown Convention Center, with completion in 2003. The Reliant Stadium will open for the start of the 2002 professional football season and serve as the home to the new Houston Texans NFL team.

Home to many professional sports teams, Houston has been a major player in the national and international sports scene for many years. This year was no exception. The four-time world champion Houston Comets continue to dominate the Women's National Basketball Association. The Houston Astros have won the National League's Central Division Championship four of the past five seasons. The City also hosted the Texaco/Havoline Grand Prix through the streets of downtown. This year is the fourth year of a six-year contract between the City and Championship Auto Racing Teams (CART). Estimated economic impact to the City each year is between \$25 and \$30 million, the equivalent of a major political party national convention.

Along with professional sports, Houston is home to a college football bowl game, held in the Reliant Astrodome. For the first time ever, on the day after Christmas this past year, the GalleryFurniture.com Bowl hosted teams from the Big 12 Conference and Conference USA.

The National Football League (NFL) is back in Houston. The NFL recently awarded Houston a franchise, the Houston Texans. The Texans will begin play in 2002 in the new \$310 million Reliant Stadium under construction next to the Reliant Astrodome. This stadium will be the home of the new team, as well as the Houston Livestock Show and Rodeo. Additionally, Houston will host the 2004 Super Bowl and the 2004 All Star Game.

The Metropolitan Transit Authority of Harris County (METRO) serves 1,281 square miles and operates more than 1,400 buses. METRO operates five HOV lanes, the largest barrier-separated system in the world. Looking ahead at mobility issues in the future, METRO has adopted the 2025 Transit System Plan for Mobility, which approves future implementation of new bus services and facilities and studies for advanced high capacity transit on nine regional corridors. METRO's downtown trolleys serve to reduce lunchtime traffic activity. In March 2001, METRO broke ground on a light rail system for the 7.5-mile Downtown-to-Reliant Park Corridor. The \$272 million light rail system -- which will traverse the Downtown employment center, colleges and universities, the Theater District, the Texas Medical Center, Hermann Park and the Zoo, the Museum District and Reliant Park-- will be complete by the year 2004. Powered electrically by overhead wires, the cars can reach speeds up to 66 mph if the line is extended. The system will operate two car trains each able to carry over 200 people. In addition to METRO's downtown revitalization efforts, its Millennium Mobility Plan also includes more than \$1 billion for street construction throughout the region for the next 10 years, \$1 billion for upgraded bus service, and more than \$144 million in transit access improvements to the reconstructed Katy Freeway.

A new aquatic entertainment and dining complex will be opening in downtown Houston in the future. Landry's Restaurants recently signed an agreement with the City to redevelop two city owned downtown landmarks into a unique five-acre entertainment and dining complex. Fire Station Number 1 and the historic Central Water Works Plant will be transformed into a public aquarium with 200 species of domestic and international marine life, a 400-seat seafood restaurant, a 6,000 square-foot ballroom, a casual café, a lounge, a plaza with dancing fountains, and many amusements including an aquatic 90-foot Ferris wheel and a gas powered train.

The Museum of Fine Arts, Houston (MFAH) celebrated the opening of the Audrey Jones Beck Building on March 25, 2000. The Beck Building more than doubles the museum's galleries for the display of its permanent collection and special exhibitions, and catapults the museum from the 13th to the 6th largest art museum in the nation in terms of exhibition space. Simultaneously, in the Caroline Wiess Law Building, newly designed installations showcase African gold and the art of sub-Saharan Africa, stunning examples of Asian, Oceanic, Native American and Pre-Columbian art, and masterworks of contemporary art. With over half a million in attendance annually, the Children's Museum boasts the highest attendance for a youth museum of its size in the country. The Holocaust Museum Houston Education Center and Memorial, offering free admission and open seven days a week, offers exhibitions, galleries, a library, and the Eric Alexander Garden of Hope. Founded in 1909, the Houston Museum of Natural Science ranks as the fourth most highly attended museum in the nation and the most highly attended attraction in Texas with over 2 million visitors annually. The Museum of Contemporary Art has also enhanced Houston's museum district since 1948. The Museum of Health and Medical Science, the newest addition to Houston's vibrant and engaging Museum District, currently serves over 150,000 visitors annually.

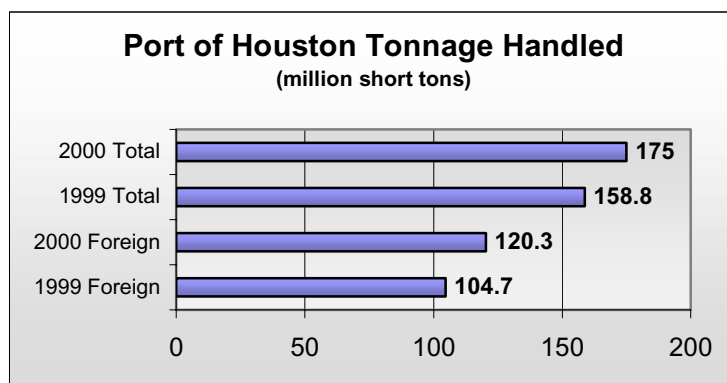
Houston is a center for cultural and performing arts with a 17-block theater district, second only in seating area to New York’s Broadway, attracting over two million people annually. The Theater District, located in Downtown Houston, is home to the Tony Award-winning Alley Theatre in addition to seven other world class theaters for the performing arts. The Houston Symphony, one of the nation’s oldest performing arts ensembles, recently celebrated its 85th season. The Symphony continues to perform in over 200 concerts a year, traveling around the U.S. and abroad. Houston Ballet is the nation’s fifth largest dance company while the Houston Grand Opera is the nation’s fifth largest opera company. The opening of the Hobby Center for the Performing Arts in Fall 2002 will further enhance the already impressive Theater District in downtown Houston.

The aerospace industry continues to be a large influence in the area. NASA/Johnson Space Center (NASA/JSC) and its contractors, including United Space Alliance, Lockheed Martin, and Boeing, continue to contribute to Houston in many ways. Receiving almost one third of NASA’s money, the Johnson Space Center contributes approximately \$2 billion to the local area economy. NASA/JSC research and development grants provide \$18.6 million to universities located within Houston. Also, NASA/JSC is constantly developing new technologies, which frequently evolve into spin-off products, and medical advances such as nanotechnology, plasma propulsion, and a new drug delivery system.

Houston has a growing tourism industry. Space Center Houston, the official visitor’s center for NASA/JSC, continues to be a popular attraction, especially now with the Johnson Space Center’s role in oversight of the creation of the international space station. The fledgling cruise industry is expected to grow with the planned construction of the Bayport Terminal at the Port of Houston, which will include a cruise terminal on the easternmost portion of the development. Currently, the cruise industry generates approximately \$40 million in revenue annually for the area. With the large and expanding airport system, and easy access to both the Caribbean and Mexico, Houston is a prime location for growth of the travel and tourism industry.

In order to keep pace with Houston’s growth, the Houston Airport System is taking on a massive expansion of Houston airport facilities estimated to cost \$2.1 billion. These improvements to what is already the world’s 6th largest multi-airport system will be accomplished at no expense to the taxpayer. Both Bush IAH and Houston Hobby airports are slated for extensive improvements. Bush is currently building new parking facilities and is preparing to build two new runways, terminal expansions, and other improvements to help prepare Houston for future growth. Hobby will receive runway improvements and upgrades along with a terminal rebuild to benefit travelers and make the airport more efficient. Ellington Field also is marked for runway improvements and cargo hangers.

The Port of Houston, ranked second in total tonnage in the nation and eighth in the world, has been and continues to be one of the primary catalysts for the future strength and development of not only Harris County, but all of southeast Texas. The Port is a large and diverse economic entity of private and public terminals, both of which contribute \$7.7 billion annually



to the region's economy. Nearly 205,000 jobs depend on cargo moving along the Houston Ship Channel. As the nation's leading port in foreign cargo, the Port of Houston's prominence helps to solidify Houston's status as an international city. The Port's productive growth in container traffic has prompted the Port Authority Commission to plan for the development of a new container terminal in southeast Harris County, the Bayport Terminal Project. The project will provide 28,580 jobs, road improvements, and environmental enhancements, as well as expanding the capacity of the Port for future growth. In the end, phases one and two of the project should have a total economic impact of \$633 million for the Houston area.

Houston also holds on strong to its Texas culture while maintaining its national and international economic dominance. Besides being an annual stop for the Professional Bull Riders circuit, the Houston Livestock Show and Rodeo (HLSR) brings together the City of Houston each year in a festival celebrating our regional culture. The Houston Livestock Show and Rodeo not only helps to keep Texas traditions and culture a part of Houston, it gives back to the community. HLSR generates a direct economic impact of over \$70 million annually and works hard to support children and education in Houston and Texas. The show attracted visitors from 44 foreign countries in 2001, and general attendance was 1.3 million. This year, as HLSR continues to grow, it gave almost \$3 million in college scholarships to Houston area youth, along with other scholarships and educational programs for students throughout Texas.

Houston is a finalist in yet another first as host to the 2012 Olympic Games. The effort is spearheaded by the Houston 2012 Foundation, a non-profit organization created for the purpose of bidding to become the U.S. Candidate City for the Olympic Games of the XXX Olympiad in the year 2012. The Foundation's efforts are aimed at securing public and private sector support and resources to promote elite amateur sporting events, such as the World Amateur Boxing Championship and the Camino Real Equestrian Events. In addition, the Foundation supports and/or participates in various educational and cultural events throughout the greater Houston area.

Communities throughout Houston continue to flourish. In an effort to improve long-neglected areas near downtown, the City is supporting a multi-million dollar redevelopment of an eighty-block section of the Fourth Ward historical area. Redevelopment will include infrastructure improvements and the construction of several hundred new homes. Growth continues in the Clear Lake area with construction of new businesses around Baybrook Mall, the area's 1.1 million square foot shopping center.

Financial Information

Accounting System and Budgetary Control

The Mayor serves as the Chief Executive of the City. The City Controller is the second highest elected official within City government and serves as the City's Chief Financial Officer. The legislative body of the City is the City Council, which consists of nine district members and five at-large members. The Mayor, City Controller, and Council Members are limited to three two-year elected terms.

The accounting system of the City is organized and operated on the basis of funds and account groups, each of which is in a separate set of self-balancing accounts which comprise each fund's assets, liabilities, fund balance, revenues and expenses. The accounting and financial reporting policies of the City included in this report conform to GAAP and reporting standards as promulgated by GASB, the American Institute of Certified Public Accountants (AICPA) and

other appropriate sources. The financial statements of the General, Special Revenue, Debt Service, Capital Projects, and Expendable Trust Funds are prepared on the modified accrual basis of accounting, whereby revenues are recorded when they become both measurable and available to finance expenditures of the current period. Expenditures are generally recorded when goods or services are received and actual liabilities are incurred and become payable with expendable available financial resources. The financial statements of the Enterprise, Internal Service, and the Fiduciary Pension, Trust and Agency Funds are prepared on the accrual basis of accounting whereby revenues/additions are recorded at the time they are earned and expenses/deductions are recorded when liabilities are incurred. Encumbrance accounting, under which purchase orders, contracts, approved requisitions and other commitments for the expenditure of funds are recorded to reserve that portion of the applicable appropriation. Outstanding encumbrances lapse at year-end. Open encumbrances are then reestablished in the succeeding fiscal year against that fiscal year's appropriations. Encumbrances do not constitute expenditures or liabilities.

The City's management is responsible for establishing and maintaining a system of internal controls designed to provide reasonable, but not absolute assurance, that the assets of the City are protected from loss, theft, or misuse and the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived and that the evaluation of costs and benefits requires estimates and judgments by management.

As a part of its internal control structure the City is required to adopt a balanced budget each year. Based upon recommendations by the Mayor, City Council adopts an annual budget for the General Fund, Debt Service Fund, and Special Revenue Funds. Exceptions are the Grant Revenue, Disaster Recovery, Health Special and Housing Special Revenue Funds, for which City Council adopts separate operating or program budgets throughout the year. Also, based upon the Mayor's recommendations, City Council adopts an annual budget for maintenance and operating expenses, excluding depreciation, debt service, and other capital costs of the proprietary funds, except for the Sports Arena, which is managed under a long-term contract. The City Council also appropriates available resources to authorize expenditures pursuant to those budgets. The City does not budget Capital Projects and other expenditures annually. Instead, City Council authorizes these expenditures through individual appropriation ordinances. No City expenditures may be made without a duly adopted ordinance. City Council can legally appropriate only those amounts of money that the City Controller has previously certified.

Although the legal level of budgetary control is the departmental level within a fund, the City maintains internal budgetary control at the expenditure category (i.e., Personnel Services, Supplies, Other Services and Capital Outlay). Budget control is primarily managed using an automated encumbrance and accounts payable system.

The City is required to undergo an annual Single Audit in conformity with the provisions of the Single Audit Act, the U. S. Office of Management and Budget Circular A-133, "Audits of State, Local Governments and Non-profit Organizations," and the State of Texas Single Audit Circular. These audits are conducted simultaneously with the City's annual financial statement audit. Information related to these Single Audits, including the schedules of financial assistance, findings and recommendations, and auditors' reports on the internal control structure and compliance with applicable laws and regulations is included in separate Single Audit Reports.

General Government Functions

General Government Revenues

Following is a table of General, Special Revenue, Debt Service, and Capital Projects Funds revenues for fiscal years ended June 30, 2001 and 2000. Revenues increased \$123 million or 8.7% from the \$1.4 billion generated in 2000 to \$1.5 billion in 2001. The General Fund accounts for all revenues and expenditures, which are not restricted, and therefore accounted for, in another fund. Special Revenue Funds account for the proceeds of specific revenues sources other than expendable and nonexpendable trust and capital projects that are restricted to expenditures for special purposes. The Debt Service Fund is used to account for all principal and interest payments on long-term debt other than that issued and serviced by Enterprise Funds. The Capital Projects Fund accounts for all resources used for the acquisition and or construction of capital facilities except those financed by Enterprise Funds. The following table presents a summary of revenues by major sources of these funds. The amount and percentage of revenue increases and decreases from fiscal year 2001 to fiscal year 2000 are also shown.

General Government Revenue by Sources (in thousands)

Revenue by Source	FY 2001 Amount	% of Total	FY 2000 Amount	Increase (Decrease) From FY 2000	% Increase (Decrease) From FY 2000
General property taxes	\$ 572,432	37.1%	\$542,777	\$29,655	5.46%
Sales tax	329,705	21.4%	313,864	15,841	5.05%
Franchise fees	175,758	11.4%	147,349	28,409	19.28%
Other taxes	7,376	0.5%	6,740	636	9.44%
Interfund billings	56,283	3.6%	55,450	833	1.50%
Fines and forfeits	43,035	2.8%	43,977	(942)	-2.14%
Licenses and permits	31,606	2.0%	30,621	985	3.22%
Charges for services	71,881	4.7%	70,680	1,201	1.70%
Investment income	28,495	1.8%	16,692	11,803	70.71%
Industrial assessments	16,906	1.1%	17,614	(708)	-4.02%
Miscellaneous	34,880	2.3%	21,085	13,795	65.43%
Intergovernmental -- grants	175,769	11.4%	153,804	21,965	14.28%
Contributions	-	0.0%	154	(154)	-100.00%
Total	\$1,544,126	100.0%	\$1,420,807	\$123,319	8.68%

The overall increase of 8.7%, from \$1.4 billion in fiscal year 2000 to \$1.5 billion in fiscal year 2001 is due to the general overall positive economic conditions experienced locally through June 30, 2001. The increase in taxable assessed value from \$80,691,551 in 2000 to \$87,683,188 in 2001, due in part to completion of new residential and commercial projects along with significant increases in property values, resulted in property taxes increasing by 5.5%. Sales tax revenues increased 5% over fiscal year 2000, due to the continued strong local economic conditions. Additionally, franchise fees increased by \$28.4 million due to an increase in the price of natural

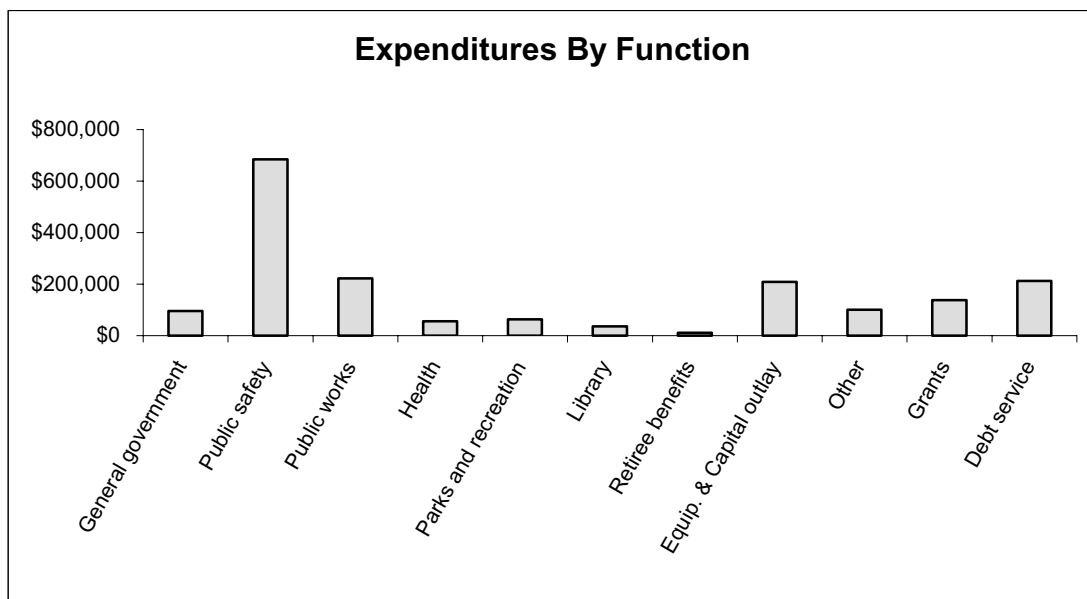
gas resulting in increases for both gas and electric franchise fees. Primarily because of unrealized appreciation in fair value from cost, investment income increased by \$12 million. Miscellaneous revenue increased by \$14 million primarily due to insurance proceeds received in connection with Tropical Storm Allison. Intergovernmental Grant revenues increased \$22 million as a result of additional grants being applied for, mainly related to Police.

Expenditures by Function

The following table presents expenditures for major functions compared to the preceding year:

General Government Expenditures by Major Functions (in thousands)

Function	2001	% of Total	2000	Increase (Decrease)	% Increase (Decrease)
General government	\$95,279	5.21%	\$96,111	(\$832)	-0.87%
Public safety	684,644	37.46%	672,737	11,907	1.77%
Public works	221,757	12.13%	219,300	2,457	1.12%
Health	55,857	3.06%	56,547	(690)	-1.22%
Parks and recreation	62,742	3.43%	61,778	964	1.56%
Library	36,240	1.98%	35,758	482	1.35%
Retiree benefits	11,675	0.64%	9,597	2,078	21.65%
Equip. & Capital outlay	209,068	11.44%	188,429	20,639	10.95%
Other	100,772	5.51%	35,089	65,683	187.19%
Grants	137,767	7.54%	111,158	26,609	23.94%
Debt service	212,066	11.60%	198,656	13,410	6.75%
Total	\$1,827,867	100.00%	\$1,685,160	\$142,707	8.47%



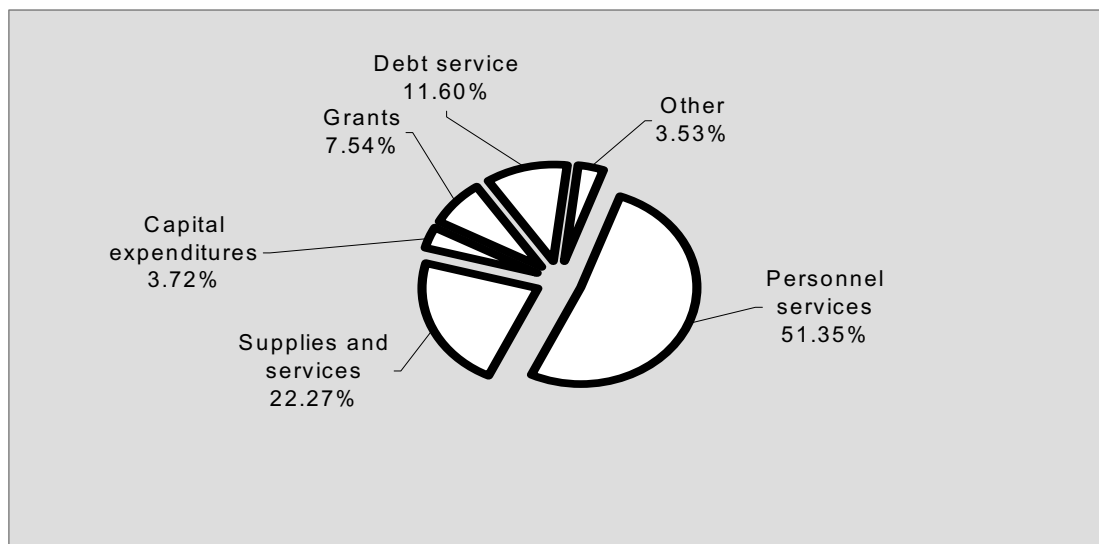
Expenditures of the General, Special Revenue, Debt Service and Capital Projects Funds increased 8.5% to \$1.8 billion in fiscal year 2001 from \$1.7 billion in fiscal year 2000. Public Safety expenditures increased \$12 million due to compensation increases in both the Police and Fire Departments. The capital outlay increase of \$21 million is primarily due to the purchase of a building by a special revenue fund and upgraded or new systems in the general government computer systems. Other expenditures increase by \$66 million because of the cost of cleanup after Tropical Storm Allison. Grant expenditures increased principally due to the cost associated with the increased Police grants received. The \$13 million increase in debt service reflects the additional payments associated with the net increase in General Obligation Debt of approximately \$38.2 million.

Expenditures by Category

These same expenditures are reflected by category in the following table:

General Government Expenditures by Category (in thousands)

Category	FY 2001 Amount	% of Total	FY 2000 Amount	Increase (Decrease) From FY 2000	% Increase (Decrease) From FY 2000
Personnel services	\$ 938,566	51.35%	\$ 928,513	\$10,053	1.08%
Supplies and services	407,111	22.27%	388,516	18,595	4.79%
Capital expenditures	67,919	3.72%	56,781	11,138	19.62%
Grants	137,767	7.54%	111,158	26,609	23.94%
Debt service	212,066	11.60%	198,656	13,410	6.75%
Other	64,438	3.53%	1,536	62,902	4095%
Total	\$ 1,827,867	100.00%	\$1,685,160	\$142,707	8.47%



General Government Fund Balances

The fund balance of the General Fund increased \$7.4 million during fiscal year 2001 to \$91 million, which represents 6.9% of total expenditures and operating transfers out.

The Special Revenue Funds fund balances decreased \$6.7 million to \$31.1 million in fiscal year 2001, down from \$37.8 million at the end of fiscal year 2000. The largest changes occurred in the Building Inspection Fund (down \$2.8 million) and the Street Maintenance and Traffic Control Fund (down \$4.6 million). The Fire Prevention Special Revenue, the Industrial Fire Training, the Street Maintenance and Traffic Control Fund, and the Sign Abatement and Community Beautification funds were closed and fund balances transferred to the General Fund at year-end.

The fund balance in the Debt Service Fund does not result from operations but from scheduled inter-fund transfers in anticipation of debt service payments. The fund balance at June 30, 2001, was \$89.6 million. This amount will cover the first seven months of principal and interest payments due in fiscal year 2002 on tax-supported debt.

The City maintains Capital Projects Funds to account for general government capital improvements funded primarily by general obligation bond proceeds. In fiscal year 2001, the City issued commercial paper and certificates of obligation for construction in the amount of \$112 million and spent \$150.6 million on general improvements, including \$63.2 million for streets and bridges. At June 30, 2001, \$57.9 million remained in the Capital Projects Fund for future capital improvements.

Proprietary Fund Types

Enterprise Funds

These funds account for City operations that are financed and operated in a manner similar to private business enterprises, where the cost of providing goods or services to the general public is financed primarily through user charges. The Airport System Fund accounts for operations of the City's airports, George Bush Intercontinental, William P. Hobby and Ellington Field. The Sports Arena Fund accounts for the City's interest in the Compaq Center, a multi-purpose sports arena leased to an independent operator. The Convention & Entertainment Facilities Fund accounts for operations of the City's entertainment centers, including the George R. Brown Convention Center, the Wortham Theater, Bayou Place, and City-owned parking garages. The Water and Sewer System Fund accounts for the production and transmission of water, and the treatment of wastewater in the Houston area. Following is certain comparative data on the enterprise funds.

Airport System Fund - Comparative Data (in thousands)

	FY 2001	FY 2000	% Change Increase (Decrease)
Total revenues	\$235,250	\$218,911	7.5%
Operating income (loss)	47,170	49,303	-4.3%
Net revenues available for debt service	112,656	105,469	6.8%
Debt service requirement	50,027	38,455	30.1%
Revenue bond coverage (net revenues available for debt service divided by annual debt service)	X 2.25	X 2.74	-17.9%
Net cash flows from operating activities	\$95,214	\$93,306	2.0%

Most of the positive increases resulted from increased passenger activity and revenue from increased concession activity. The Airport System's current liabilities arising from operations and its two-month maintenance and operating reserve are fully funded with cash and investments.

Sports Arena

The Sports Arena Fund accounts for certain net lease revenues from the City's interest in the Compaq Center, a 16,729-seat multi-purpose sports facility. Construction of the facility was financed primarily by conduit debt consisting of first mortgage revenue bonds guaranteed by the operating company. Under the lease agreement, the operator is responsible for the operations of the facility and for principal and interest payments on the bonds. This agreement is for the life of the bonds and does not require any cash contributions from the City. The bonds will be entirely repaid by fiscal year 2004.

Convention & Entertainment Facilities Fund – Comparative Data (in thousands)

	FY 2001	FY 2000	% Change Increase (Decrease)
Total revenues	\$73,619	\$63,160	16.56%
Operating income (loss)	(9,218)	(9,735)	-5.31%
Hotel occupancy tax (non-operating Revenue)	46,123	42,550	8.40%
Net cash flows from operating activities	(\$1,154)	(\$11,680)	-90%

The operating loss does not include non-operating hotel tax revenues, which increased from \$42.5 to \$46.1 million or 8.4%. Cash flows from operating activities increased principally as a result of timing differences in the flow of funds to a component unit.

Water and Sewer System Fund – Comparative Data (in thousands)

	<u>FY 2001</u>	<u>FY 2000</u>	<u>% Change Increase (Decrease)</u>
Total revenues	\$626,717	\$616,698	1.62%
Operating income (loss)	41,730	124,934	-66.60%
Net revenues available for debt service	324,892	347,166	-6.42%
Debt service requirement	218,978	212,151	3.22%
Revenue bond coverage (net revenues available for debt service divided by annual debt service)	X 1.48	X 1.64	-9.76%
Net cash flows from operating activities	\$323,281	\$346,543	-6.71%

The System's current liabilities arising from operations are fully funded, and its one-month maintenance and operating reserve is fully funded with cash and investments. Revenues decreased primarily due to record rainfall during the fiscal year, and maintenance and operating cost increased primarily due to higher utility cost and excessive water line breaks during the summer months of 2000.

Fiduciary Fund Types

Pension Trust Funds

The Houston Firefighter's Relief and Retirement Fund reports an actuarial accrued liability of \$1.6 billion. Of this, \$137 million is over funded based on the actuarial value of assets to \$ 67.9 million over funded in the previous year. The Houston Municipal Employees Pension Plan reports an actuarial accrued liability of \$1.5 billion. Of that, \$133.4 million is unfunded based on the actuarial value of assets compared to \$117.7 million unfunded in the previous year. As of July 1999, the Houston Police Officers Pension Plan reports an actuarial accrued liability of \$1.7 billion. Of that, \$27.5 million is unfunded based on the actuarial value of assets, compared to \$31.3 million unfunded in the previous year. The Board of Trustees has not adopted an actuarial valuation report subsequent to July 1999. The City's contributions to the pension plans are actuarially determined; the result is contribution rates that, over time, remain level as a percent of payroll.

Risk Management

The City purchases commercial property insurance covering city buildings and contents, including abandoned/vacant facilities and leased locations, business interruption/extra expense coverage for the Aviation and Convention and Entertainment Departments. The City also purchases boiler and machinery insurance to provide coverage for loss caused by mechanical or electrical equipment breakdown, including damage to the equipment, damage to other property of the insured, and damage to property of others. The City is self-insured for its employee health benefit plan, long term disability plan, workers' compensation and third-party liability claims.

Employee Health and Long-Term Disability Benefits

The City accounts for its health care and long-term disability plans in internal service funds with full accrual accounting. As of June 30, 2001, these funds were substantially funded for both reported claims and those that were incurred and not yet reported. The new health contract is in effect from May 2001 through April 2004, with two one-year options. Because under the prior contract increases were capped at the CPI, costs increased significantly. The recommended delivery system and plan design modifications in the first contract year allow the City of Houston to keep cost down to an increase of 28% over the prior 12-month amount. Plan costs in subsequent years are capped at 15% each of years two and three and 20-25% in each of the two option years. The actual rate of increase in the option years is based on a prescribed formula associated with actual cost increases.

Workers' Compensation

The City's workers' compensation program is self-insured. All indemnity medical and expense payments are funded by charge-backs to the operating departments. Costs are funded as payments are made. At June 30, 2001, the unfunded long-term liability for incurred claim costs of the governmental funds was \$39.2 million, compared to \$33.4 million at June 30, 2000. Total liability for all funds increased to \$49.5 million, compared to \$43.7 million last year. Claims costs attributable to the City's enterprise funds are fully funded. Claims paid for the entire workforce were \$22.2 million. The City uses a third party administrator for claims processing and payment services to provide statutory benefits to its employees.

Debt Administration

The City continues to issue commercial paper during the construction period for most its capital improvement programs. The commercial paper program remains the most efficient and cost-effective method of initially financing new capital projects until permanent financing is arranged. The program has also helped in reducing the City's arbitrage rebate liability.

During the fiscal year the Houston Airport System issued \$696 million in bonds, of which \$606 million constituted new money to fund airport expansion and improvements, and \$90 million was used to retire outstanding commercial paper. During the fiscal year the City of Houston Convention and Entertainment Facilities Department issued a total of \$626.5 million in bonds to fund the construction of a new convention center hotel, a parking garage, expansion of the George R. Brown Convention Center, and to refund existing debt of \$150 million. Also during the fiscal year the Water and Sewer System issued bonds to refund \$278 million of commercial paper into long-term debt, and Public Improvement Bonds were issued in the amount of \$208 million to retire \$190 million of general obligation commercial paper into long-term debt, and to refund \$18 million of Public Improvement Bonds for present value savings.

Cash Management

The City Controller's Office manages the investment of all City funds, except those administered by pension boards or trustees. In meeting that responsibility, the City Controller's Office is governed by the following objectives, in order of priority: safety of principal, liquidity, return on

investment, and meeting legal requirements. All of these objectives were satisfied during the past fiscal year.

To maximize efficiency, the City's various funds are pooled for investment purposes. As of June 30, 2001 pooled investments totaled \$ 2,514,484,000. The City's portfolios earned \$163,244,000 in fiscal year 2001, compared to \$77,998,000 in fiscal year 2000. The increased earnings are due to higher levels of bond proceeds being available for investment during fiscal 2001.

Award

The Government Finance Officers Association (GFOA) awarded a *Certificate of Achievement* for Excellence in Financial Reporting to the City for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2000. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of a state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA.

Acknowledgements

The preparation of this report on a timely basis could not have been accomplished without the dedicated services and hard work of a highly qualified staff. The City of Houston has such a staff in the City Controller's Office. Although much of the time and effort in preparation of this report lies in the Financial Reporting Division, they were supported by the other divisions of the Office: Executive, Administration, Information Systems, Operations, Investment and Debt Management, and Audit. I would like to express my appreciation to all the staff of the City Controller's Office, and to the staff of the Finance and Administration Department, Aviation Department, Convention and Entertainment, and Public Works and Engineering Department who assisted and contributed to the preparation of this report.

The City Controller's Office also received invaluable assistance and support from many others outside our immediate organization. Within the City of Houston, the accounting staffs of the operating departments and the technical staff of the Information Services Division all played key roles in producing this report. The cover photograph is courtesy of the Greater Houston Partnership. KPMG LLP was not only our independent auditor, but also served as an invaluable source of information and ideas for improving the way that City finances are reported. Finally, we acknowledge the Mayor and City Council Members who have consistently supported the City's goal of excellence in all aspects of financial management. Their support is greatly appreciated, and I look forward to working together to continue improving the City's financial condition.

Special thanks for the production of this year's CAFR are gratefully given to the City of Houston's Parks and Recreation Department. The Department's Office of Marketing and Special Events provided the CAFR design, printing assistance and the photography featured throughout

the report. I appreciate the many hours Parks' staff devoted to this effort, which helps to showcase the beauty of our diverse, international, and very green City. We are justly proud and hope that this CAFR, in offering a glimpse of this remarkable place, will encourage readers to want to see more.

A handwritten signature in black ink, reading "Sylvia R. Garcia". The signature is fluid and cursive, with the first name "Sylvia" and last name "Garcia" clearly legible.

Sylvia R. Garcia
City Controller

Sources:

ACCRA

Baseball Almanac

Census 2000

Federal Reserve Bank of Dallas

Greater Houston Convention and Visitors Bureau

Greater Houston Partnership

Houston METRO Transit Authority

Houston Texans/HOK

University of Houston Center for Public Policy

Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Houston,
Texas

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2000

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Thomas A. Brewer
President

Jeffrey L. Essler
Executive Director