Houston First Corporation

(A Component Unit of the City of Houston, Texas)

Financial Statements as of and for the Years
Ended December 31, 2013 and 2012, and
Independent Auditors' Report

HOUSTON FIRST CORPORATION
(A Component Unit of the City of Houston, Texas)

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Deloitte & Touche LLP
Suite 4500
1111 Bagby Street
Houston, TX 77002-4196
USA

Tel: +1 713 982 2000
Fax: +1 713 982 2001
www.deloitte.com

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Houston First Corporation
Houston, Texas

We have audited the accompanying financial statements of Houston First Corporation (the "Corporation"), which comprise the statements of net position, as of December 31, 2013 and 2012, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on the audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform that audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Corporation's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material aspects, the net position of Houston First Corporation as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Government Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Deloitte & Touche LLP

October 23, 2014

The following discussion of Houston First Corporation (the "Corporation") should be read in conjunction with the financial statements and notes thereto appearing elsewhere in this report. Historical results and trends that might appear should not be taken as indicative of future operations. The results of operations and financial condition of the Corporation, as reflected in the accompanying financial statements and related notes, are subject to management's evaluation and interpretation of business conditions, changing capital market conditions, and other factors that could affect the ongoing viability of the Corporation.

The Houston Convention Center Hotel Corporation ("Hotel Corporation") was formed on behalf of the City of Houston, Texas (the "City"), in February 2000 pursuant to Chapter 431, Subchapter D, of the Texas Transportation Code, and Chapter 394 of the Texas Local Government Code. It was organized for the specific purpose of constructing, improving, enlarging, equipping, repairing, operating, and maintaining a convention center hotel (the "Hotel") located near and connected to the George R. Brown Convention Center (the "Convention Center"). In this regard, the Hotel Corporation was responsible for overseeing the construction and development of the Hotel; a 1,600-space parking garage (the "Parking Garage"); and three skywalks connecting the Hotel, the Parking Garage, and the Convention Center (the "Project"). Construction was completed and the Project opened for business in December 2003 as the Hilton Americas–Houston (the "Hilton"). As of December 31, 2013 and 2012, Hilton Management LLC managed the Hotel through a qualified management contract (the "Management Agreement"), and Ace Parking Management managed the Parking Garage.

On June 1, 2011, the City's city council (the "City Council") approved the consolidation of the City's Convention & Entertainment Facilities Department (the "Department") into the Hotel Corporation (the "Consolidation"), effective July 1, 2011, in order to improve the coordination of the City's convention and entertainment services by bringing various entities responsible for generating and spending City hotel occupancy tax (HOT) revenues under one governing body. In connection with the Consolidation, the Hotel Corporation reconstituted and renamed itself as the "Houston First Corporation," which assumed the primary roles and responsibilities of the Department. To accomplish this, the Hotel Corporation amended its bylaws and articles of incorporation to broaden its authority to accomplish its expanded duties and responsibilities. The Corporation has the authority to exercise all rights and privileges of a Texas nonprofit corporation and, as a governmental unit within the meaning of Chapter 101 of the Texas Civil Practice Remedies Code, its operations are governmental and not proprietary functions. The Corporation is governed by the board of directors appointed and approved by the Mayor and the City Council.

The Corporation (a) leases all previously existing Department facilities and Department-managed facilities; (b) operates, manages, maintains, develops, and redevelops those existing facilities; (c) has been assigned and now administers all of the Department's obligations and responsibilities, as well as its revenue budgeted as part of the Department's budget, including, but not limited to, municipal HOT receipts, license fees, and concession revenues; and (d) as the City's agent, collects, administers, and audits HOT funds in accordance with terms of City ordinances. The City has entered into an interlocal agreement (the "Consolidation Interlocal Agreement") with the Corporation, whereby the Corporation will pay $1,380,000 per year to lease all existing Department facilities and Department-managed facilities. The Corporation also agreed to pay the City a one-time fee of $8,620,000 during the City's fiscal year ended June 30, 2012, from operating revenues of the Hotel. The Consolidation Interlocal Agreement's initial term expires on December 31, 2026, but will be extended automatically until June 30, 2041, unless canceled by either party on or before June 30, 2026.

On March 4, 2013, the Corporation formed Houston First Holdings, LLC, a wholly owned subsidiary of the Corporation, as a "special-purpose" entity for the purpose of owning, holding, selling, leasing, transferring, exchanging, operating, managing, and otherwise dealing with the Hilton and its parking garage.

For the years ended December 31, 2013 and 2012, interest earned from investments, net revenues from the operations of the Project, plus certain tax rebates collected at and remitted from operations located within the Project were sufficient to fund expenses of the Hotel Corporation, pay the monthly debt service expense, and fund the remaining obligations between the Hotel Corporation and the City.

OVERVIEW OF THE FINANCIAL STATEMENTS

The statements of net position present information on all of the Corporation's assets, deferred outflow of resources and liabilities, with the difference reported as net position. Comparisons in net position may serve as a useful indicator of whether the financial position of the Corporation is improving or deteriorating. The statements of net position can be found on page 10 of this report.

The statements of revenues, expenses, and changes in net position report the Corporation's revenues, expenses, and resulting change in net position during the period reported, regardless of when cash is received or paid. Therefore, revenues and expenses are reported in the statements of revenues, expenses, and changes in net position for some items that will affect cash flow in future fiscal years. The statements of revenues, expenses, and changes in net position can be found on page 11 of this report.

The statements of cash flows report how much cash was provided by, or used for, the Corporation's operations, investing activities, and acquisition or retirement of capital assets. The statements of cash flows can be found on pages 12–13 of this report.

The notes to the financial statements provide additional information that is essential for a complete understanding of the data in the financial statements described above. The notes to the financial statements can be found on pages 14–27 of this report.

NET POSITION

Total net position at December 31, 2013, was $97,873,970, a 57.5% increase from December 31, 2012. Total net position at December 31, 2012, was $62,128,802, a 99.2% increase from December 31, 2011.

CONDENSED STATEMENTS OF NET POSITION

DECEMBER 31, 2013, 2012, AND 2011

	December 31, 2013	December 31, 2012	December 31, 2011
Current assets	$ 129,017,360	$ 100,932,626	$ 81,583,669
Noncurrent assets	85,783,395	43,336,921	39,056,583
Capital assets	219,882,419	221,444,817	222,658,969
Total assets	$ 434,683,174	$ 365,714,364	$ 343,299,221
Deferred outflow of resources	$ 1,580,743	$ 1,661,106	$ 406,397
Current liabilities	$ 40,016,562	$ 48,321,447	$ 47,619,133
Long-term liabilities	298,373,385	256,925,221	264,901,126
Total liabilities	$ 338,389,947	$ 305,246,668	$ 312,520,259
Net position	$ 97,873,970	$ 62,128,802	$ 31,185,359

Total assets increased $68,968,810 to $434,683,174 at December 31, 2013, from $365,714,364 at December 31, 2012. This increase is primarily a result of the initial draw on the new mortgage loan with The Variable Annuity Life Insurance Company (VALIC) more fully described in Note 6. Of the initial $50 million draw, $31,897,494 represents an increase in due from affiliate and $10,689,626 represents an increase in deposits held by others. The remaining increase in cash and cash equivalents of $8,887,594 and increase in short-term equity in pooled investments of $17,817,679 was the result of operations and unspent proceeds of the loan.

Total assets increased $22,415,143 to $365,714,364 at December 31, 2012, from $343,299,221 at December 31, 2011. Of this increase, $18,842,542 is in short-term equity in pooled investments and $2,281,266 is in cash and cash equivalents, and it is attributable to working capital and reserve transfers authorized in the Consolidation, HOT funds held as agent for the City, and cash generated from operations.

In May 2001, the City issued Hotel Occupancy Tax and Special Revenue Bonds, Series 2001 A and B, and Hotel Occupancy Tax Special Revenue Adjustable Rate Bonds, Series 2001 C (collectively referred to as the “Bonds”), which provided the permanent funding for the payment of the total cost of the Project incurred by the Corporation. Proceeds of the Bonds allocated for the Project were loaned by the City to the Corporation and evidenced by a note payable. As of year-end, amounts held in the debt service reserve funds were the only remaining unspent proceeds from these Bonds.

On August 31, 2011, the City issued Hotel Occupancy Tax and Special Revenue Refunding Bonds, Series 2011A and 2011B. The true interest cost of the issue was 4.26%. The bonds mature in varying amounts from 2012 to 2033. Net present value savings totaled $9.4 million or 3.92% of the refunded bonds. The Series 2011B bonds were hotel-allocated bonds, and the proceeds were used to refund the hotel-allocated portions of the City’s Hotel Occupancy Tax and Special Revenue Bonds, Series 2001 A and B, to convert a portion of the Hotel Occupancy Tax Special Revenue Adjustable Rate Bonds, Series 2001C variable-rate debt to fixed-rate debt, and to fund an additional deposit to the debt service reserve fund. As of both December 31, 2013 and 2012, the amount of the note that is amortized based on City-issued variable-rate debt was

$75 million, with the remainder based on City-issued fixed-rate debt. The variable-rate debt has been issued as seven-day auction rate securities with 10% being the maximum interest rate permitted.

On August 15, 2012, the City issued $41,525,000 of Convention & Entertainment Facilities Department Hotel Occupancy Tax (HOT) and Special Revenue Refunding Bonds, Series 2012 with 5% coupons. The true interest cost was 4.80%. The bonds mature in varying amounts from 2026 to 2033. Proceeds were used to refund $41,245,000 of the Series 2001B2 Convention & Entertainment HOT and Special Revenue Refunding Bonds. Net present value savings totaled $1.9 million or 4.67% of the refunded bonds and reduced total debt service by $2.3 million.

Funds held by the City, listed as equity in pooled investments — restricted, include the debt service reserve funds, the debt service funds, and tax rebates and are invested in the City's general investment pool. The amount of the investments held by the City was $34,117,687 and $35,027,021 at December 31, 2013 and 2012, respectively.

The Corporation made principal payments totaling $9,875,000 and $12,720,000 in 2013 and 2012, respectively. The total notes payable balance includes the Corporation's allocable portion of the unamortized bond premiums, net of discounts, which totaled $4,141,080 and $5,467,632 at December 31, 2013 and 2012, respectively. The net amortization on the premiums and discounts totaled $1,326,552 and $1,424,790 for the years ended December 31, 2013 and 2012, respectively. Accumulated amortization of the bond premiums, net of discounts, totaled $3,266,515 and $1,939,963 at December 31, 2013 and 2012, respectively. The Corporation funds 1/12th of the annual principal payment each month so that, on September 1 of each year, the full principal amount will be available for payment. The Corporation did not borrow additional amounts from the City during 2013 or 2012.

Total liabilities increased $33,143,279 to $338,389,947 in 2013 from $305,246,668 in 2012, which was primarily attributable to the initial draw of $50 million on the new mortgage loan offset by the principal payment on the hotel allocated bonds of $9,875,000 and a decrease in due to the City of $7,338,669.

Total liabilities decreased $7,273,591 to $305,246,668 in 2012 from $312,520,259 in 2011, which was primarily attributable to the principal payments of debt.

The Corporation's net position increased $35,745,168 to $97,873,970 at December 31, 2013, from $62,128,802 at December 31, 2012. Of this increase, $68,968,810 is attributable to an increase in assets offset primarily by an increase of $33,143,279 liabilities as described above.

The Corporation's net position increased $30,943,443 to $62,128,802 at December 31, 2012, from $31,185,359 at December 31, 2011. Of this increase, $22,415,143 is attributable to an increase in assets and $7,975,905 is attributable to a decrease in long-term debt as described above.

CONDENSED STATEMENTS OF CHANGES IN NET POSITION

DECEMBER 31, 2013, 2012, AND 2011

	December 31, 2013	December 31, 2012	December 31, 2011
OPERATING REVENUES:			
Hotel revenues	$ 88,910,489	$ 82,296,639	$ 71,124,882
Venue revenues	19,018,928	16,711,814	4,745,362
Parking revenues	5,583,320	4,704,900	4,147,261
Other operating revenues	3,584,231	3,552,799	3,623,772
Total operating revenues	117,096,968	107,266,152	83,641,277
OPERATING COSTS AND EXPENSES:			
Hotel expenses:			
Direct expenses	30,390,051	28,781,196	25,875,289
Management fees	3,881,890	3,525,818	3,149,669
Depreciation	9,057,292	8,990,539	7,835,057
General and administrative	21,731,301	22,284,187	20,046,557
Lease expense	1,671,583	1,650,215	1,419,675
Other hotel expenses	1,939,441	3,678,566	3,648,009
Parking expenses	4,683,492	2,107,454	1,134,313
Venue expenses:			
Direct expenses	30,516,372	28,985,037	14,720,043
Depreciation and amortization	478,632	215,000	-
General and administrative	7,898,581	8,945,209	4,034,341
Total operating costs and expenses	112,248,635	109,163,221	81,862,953
OPERATING INCOME (LOSS)	4,848,333	(1,897,069)	1,778,324
NONOPERATING REVENUES (EXPENSES):			
Allocation of garage income to the City of Houston	-	-	(664,104)
Other income	-	110,668	657,622
Tax rebates	10,317,165	9,799,524	8,651,773
Transfers from primary government	67,584,899	64,266,743	53,169,726
GHCVB contract expense	(17,602,125)	(15,610,063)	(7,241,886)
Sponsorship expense	(2,900,531)	(3,091,807)	(1,458,707)
Transfers to primary government	(17,189,549)	(14,769,257)	(10,623,736)
Interest expense	(9,921,021)	(8,368,772)	(9,132,172)
Interest income	607,997	503,476	274,477
Total nonoperating revenues (expenses)	30,896,835	32,840,512	33,632,993
CHANGE IN NET POSITION	35,745,168	30,943,443	35,411,317
NET POSITION — Beginning of year	62,128,802	31,185,359	(4,225,958)
NET POSITION — End of year	$ 97,873,970	$ 62,128,802	$ 31,185,359

1. Operating Revenues

Total operating revenues for 2013 and 2012 were $117,096,968 and $107,266,152, respectively, resulting in an increase of $9,830,816. The majority of the increase in operating revenues for 2013 was attributable to an increase in room revenue at the Hotel. The remaining increase was from an increase in facility rental and parking revenues.

Total operating revenues for 2012 increased $23,624,875 from $83,641,277 in 2011 to $107,266,152 in 2012. The increase in operating revenues was primarily (51%) attributable to the recognition of a full year of revenue versus six months of revenue from the leased venues as a result of the Consolidation, with the remaining increase due to an increase in room revenue at the Hotel.

2. Tax Rebates

Tax rebates increased $517,641 from $9,799,524 in 2012 to $10,317,165 in 2013 and increased $1,147,751 from $8,651,773 in 2011 to $9,799,524 in 2012. The increase in both years was primarily due to the growth in HOT revenues, which was directly related to the increase in room revenue described in (1) above.

3. Transfers from Primary Government

In the Consolidation Interlocal Agreement, the City assigned to the Corporation the net available pledged revenues to pay for operating expenses, capital expenditures, and for any other lawful purpose. The transfers represent the HOT and pledged parking revenues remaining after debt service and other debt-related expenses that were paid, the remaining initial working capital transfer, and the transfer of other remaining Department fund balances. For 2013, the amount transferred from the Department was $67,584,899, an increase of $3,318,156 from 2012. The increase is from the increase in HOT revenues and parking revenues at the City. For 2012, the amount transferred from the Department was $64,266,743, an increase of $11,097,017 from 2011. The increase is due to a full year of transfers recorded in 2012, plus an additional transfer of $5,189,523 related to initial working capital from the City.

4. Operating Costs and Expenses

Total operating costs and expenses increased $3,085,414 from $109,163,221 in 2012 to $112,248,635 in 2013 and increased $27,300,268 from $81,862,953 in 2011 to $109,163,221 in 2012. The increase in 2013 and 2012 is primarily due to an increase in direct operating expenses and management fees.

Direct operating expenses related to hotel, parking, and leased venue operations increased $3,998,471 from $65,202,468 in 2012 to $69,200,939 in 2013. The increase is directly related to the increase in operating revenues.

Direct operating expenses related to hotel, parking, and leased venue operations increased $18,405,139 from $46,797,329 in 2011 to $65,202,468 in 2012. Approximately 77% of the increase was attributable to a full year of leased venue direct expenses in 2012 versus six months in 2011. The remaining increase in direct expenses was realized through hotel operations, including the $1,380,000 annual lease payment to the City, and was proportionate to the increase in hotel operating revenues.

Direct operating expenses related to hotel operations as a percentage of hotel operating revenues were 34% and 35% in 2013 and 2012, respectively.

Management fees increased $356,072 from $3,525,818 in 2012 to $3,881,890 in 2013 and increased $376,149 from $3,149,669 in 2011 to $3,525,818 in 2012. The increase in both years is based on the formula provided in the management fee rider of the Management Agreement.

The Corporation's operating income before depreciation totaled $14,384,257 and $7,308,470 in 2013 and 2012, respectively. The Corporation's depreciation expense for 2013 and 2012 totaled $9,535,924 and $9,205,539, respectively.

The Corporation's operating income (loss), which includes the noncash charge of depreciation, totaled $4,848,333 and $(1,897,069) in 2013 and 2012, respectively.

5. General and Administrative Expenses

In 2012 and 2013, general and administrative expenses were incurred from both hotel and leased venue operations. General and administrative expenses decreased $1,599,514 to $29,629,882 in 2013 from $31,229,396 in 2012. The majority of the decrease is attributable to expiring convention service agreements. General and administrative expenses increased $7,148,498 from $24,080,898 in 2011 to $31,229,396 in 2012. The increase in 2012 was attributable to the recognition of a full year of expenses versus six months from the leased venues as a result of the Consolidation.

6. Transfers to Primary Government

In the Consolidation Interlocal Agreement, the Corporation agreed to make certain payments to the City for obligations previously paid directly by the Department. At December 31, 2013, those payments totaled $17,189,549. At December 31, 2012, payments of $14,769,257 were made to the City. As one of the payments is based on HOT revenues, the increase of $2,420,292 in 2013 and the increase of $4,145,521 in 2012 were directly related to the increase in HOT revenues for those respective years.

7. Interest Expense

Interest expense increased $1,552,249 from $8,368,772 in 2012 to $9,921,021 in 2013. The increase in interest expense was primarily due to the new borrowing of $50 million. Interest expense decreased $763,400 from $9,132,172 in 2011 to $8,368,772 in 2012. The decrease was primarily due to lower variable interest rates on the note payable to the City in 2012.

8. Greater Houston Convention and Visitors Bureau (GHCVB) Contract Expense

GHCVB contract expense increased $1,992,062 from $15,610,063 in 2012 to $17,602,125 in 2013. As the contract payment is based on HOT revenues, the increase was directly related to the increase in 2013 HOT revenues.

GHCVB contract expense increased $8,368,177 from $7,241,886 in 2011 to $15,610,063 in 2012. The increase was attributable to payments for 12 months in 2012 versus six months in 2011 as a result of the Consolidation.

HOUSTON FIRST CORPORATION
(A Component Unit of the City of Houston, Texas)

STATEMENTS OF NET POSITION
DECEMBER 31, 2013 AND 2012

	2013	2012
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 60,880,109	$ 51,992,515
Accounts receivable — net	3,573,007	3,903,477
Tax rebates receivable	1,479,321	1,868,712
Prepaid expenses and other assets	1,460,818	1,346,988
Deposits held by others - current	1,985,492	-
Short-term equity in pooled investments	59,638,613	41,820,934
Total current assets	129,017,360	100,932,626
NON-CURRENT ASSETS:		
Due from affiliate	32,820,129	-
Deposits held by others — restricted	10,827,052	-
Equity in pooled investments — restricted	34,117,687	35,027,021
Property, plant, and equipment — net	219,882,419	221,444,817
Other assets — net	8,018,527	8,309,900
Total non-current assets	305,665,814	264,781,738
TOTAL ASSETS	434,683,174	365,714,364
DEFERRED OUTFLOW OF RESOURCES — Deferred amounts from debt refunding	1,580,743	1,661,106
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	14,326,779	12,522,990
Accrued interest	2,646,441	2,931,293
Accrued expenses	9,507,924	9,658,077
Due to City of Houston	4,958,383	12,297,052
Current portion of notes payable	7,840,000	9,875,000
Current portion of unearned revenue	337,035	637,035
Current portion of inducement fee from Hotel Operator	400,000	400,000
Total current liabilities	40,016,562	48,321,447
LONG-TERM LIABILITIES:		
Notes payable	277,956,080	237,122,632
Unearned revenue	9,408,896	9,745,931
Inducement fee from Hotel Operator	1,566,667	1,966,667
Subordinated management fee	9,441,742	8,089,991
Total long-term liabilities	298,373,385	256,925,221
Total liabilities	338,389,947	305,246,668
COMMITMENTS AND CONTINGENCIES (Note 8)		
NET POSITION		
Net investment in capital assets	2,589,944	(6,746,203)
Restricted for debt service	14,996,850	15,157,828
Unrestricted	80,287,176	53,717,177
TOTAL NET POSITION	$ 97,873,970	$ 62,128,802

See notes to the financial statements.

HOUSTON FIRST CORPORATION
(A Component Unit of the City of Houston, Texas)

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	2013	2012
OPERATING REVENUES:		
Hotel revenues	$ 88,910,489	$ 82,296,639
Venue revenues	19,018,928	16,711,814
Parking revenues	5,583,320	4,704,900
Other operating revenues	3,584,231	3,552,799
Total operating revenues	117,096,968	107,266,152
OPERATING COSTS AND EXPENSES:		
Hotel expenses:		
Direct expenses	30,390,051	28,781,196
Management fees	3,881,890	3,525,818
Depreciation and amortization	9,057,292	8,990,539
General and administrative	21,731,301	22,284,187
Lease expense	1,671,583	1,650,215
Other hotel expenses	1,939,441	3,678,566
Parking expenses	4,683,492	2,107,454
Venue expenses:		
Direct expenses	30,516,372	28,985,037
Depreciation and amortization	478,632	215,000
General and administrative	7,898,581	8,945,209
Total operating costs and expenses	112,248,635	109,163,221
OPERATING INCOME (LOSS)	4,848,333	(1,897,069)
NONOPERATING REVENUES (EXPENSES):		
Other income	-	110,668
Tax rebates	10,317,165	9,799,524
Transfers from primary government	67,584,899	64,266,743
GHCVB contract expense	(17,602,125)	(15,610,063)
Sponsorship expense	(2,900,531)	(3,091,807)
Transfers to primary government	(17,189,549)	(14,769,257)
Interest expense	(9,921,021)	(8,368,772)
Interest income	607,997	503,476
Total nonoperating revenues (expenses)	30,896,835	32,840,512
INCREASE IN NET POSITION	35,745,168	30,943,443
NET POSITION — Beginning of year	62,128,802	31,185,359
NET POSITION — End of year	$ 97,873,970	$ 62,128,802

See notes to the financial statements.

HOUSTON FIRST CORPORATION
(A Component Unit of the City of Houston, Texas)

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	$ 117,192,091	$ 109,847,731
Cash payments to suppliers for goods and services	(62,034,724)	(57,568,209)
Cash payments to employees for services	(38,328,124)	(37,987,794)
Cash transfers from the City per agreements	60,246,230	62,871,229
Cash payments to the City per agreements	(18,070,904)	(21,089,593)
Cash payments to GHCVB	(16,362,356)	(15,244,710)
Cash payments for sponsorships	(2,900,531)	(3,091,807)
Net cash provided by operating activities	39,741,682	37,736,847
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:		
Proceeds from debt financing	31,897,494	-
Payments for interest	(1,231,795)	-
Net cash provided by non-capital financing activities	30,665,699	-
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Payments for interest	(9,085,272)	(9,295,097)
Receipt of tax rebates	9,682,215	10,667,045
Principal payment on note payable	(9,875,000)	(12,720,000)
Proceeds from debt financing	6,444,135	1,527,600
Payment for debt issuance costs	(166,250)	(468,979)
Payment for deposits held by others	(1,420,414)	-
Acquisition of property, plant, and equipment	(7,978,724)	(7,264,323)
Net cash used in capital and related financing activities	(12,399,310)	(17,553,754)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Loans to affiliates	(31,897,494)	-
Interest received on investments	(193,385)	503,476
Purchase of investments	(66,999,414)	(62,220,231)
Proceeds from sales and maturities of investments	49,969,816	43,814,928
Net cash used in investing activities	(49,120,477)	(17,901,827)
NET INCREASE IN CASH AND CASH EQUIVALENTS	8,887,594	2,281,266
CASH AND CASH EQUIVALENTS — Beginning of year	51,992,515	49,711,249
CASH AND CASH EQUIVALENTS — End of year	$ 60,880,109	$ 51,992,515

(Continued)

HOUSTON FIRST CORPORATION
(A Component Unit of the City of Houston, Texas)

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	2013	2012
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income (loss)	$ 4,848,333	$ (1,897,069)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation and amortization	9,535,924	9,205,539
Amortization of Hotel Operator fee	(400,000)	(400,000)
Increase in subordinated management fee	1,351,751	-
Decrease in accounts receivable — net	330,470	1,953,633
Increase in prepaid expenses and other assets	(113,830)	(120,735)
Increase in deposits held by others	(702,504)	-
Increase (decrease) in other assets	291,373	(4,717,575)
Increase in accounts payable	1,808,987	2,201,827
Increase in accrued expenses	874,188	900,742
Decrease in due to primary government	(7,338,669)	(1,395,514)
(Decrease) increase in current portion of unearned revenue	(637,035)	1,099,715
Nonoperating income (expenses):		
Transfers from City	67,584,899	64,266,743
Other City obligations	(17,189,549)	(14,769,257)
GHCVB contract expense	(17,602,125)	(15,610,063)
Sponsorship expense	(2,900,531)	(3,091,807)
Other income	-	110,668
Net cash provided by operating activities	$ 39,741,682	$ 37,736,847
NONCASH TRANSACTIONS:		
Capital additions included in liabilities	$ 929,048	$ 727,064
Deposits held by others funded for management and inducement fees	$ 10,689,626	

See notes to the financial statements. (Concluded)

1. ORGANIZATION

Houston First Corporation (the "Corporation") (formerly, Houston Convention Center Hotel Corporation (the "Hotel Corporation")), a component unit of the City of Houston, Texas (the "City"), was formed on February 18, 2000, under the provisions of Chapter 431, Subchapter D of the Texas Transportation Corporation Act, and Chapter 394, Vernon's Texas Codes Annotated, Local Government Code. The purpose of the Hotel Corporation was to aid and act on behalf of the City in establishing, constructing, improving, enlarging, equipping, repairing, operating, or maintaining (any or all) a 1,200-room convention center hotel in downtown Houston (such hotel to be within 1,000 feet of the George R. Brown Convention Center (the "Convention Center")) (the "Hotel") and a parking garage (the "Parking Garage") for approximately 1,600 vehicles adjacent to the Hotel. The Hotel was completed in 2003 and opened on December 4, 2003.

On June 1, 2011, City's city council (the "City Council") approved the consolidation of the City's Convention & Entertainment Facilities Department (the "Department") into the Hotel Corporation (the "Consolidation"), effective July 1, 2011, in order to improve the coordination of the City's convention and entertainment services by bringing various entities responsible for generating and spending City hotel occupancy tax (HOT) revenues under one governing body. In connection with the Consolidation, the Hotel Corporation reconstituted and renamed itself as "Houston First Corporation," and Houston First Corporation assumed the primary roles and responsibilities of the Department. To accomplish this, the Hotel Corporation amended its bylaws and articles of incorporation to broaden its authority to accomplish its expanded duties and responsibilities. The Corporation has the authority to exercise all rights and privileges of a Texas nonprofit corporation and, as a governmental unit within the meaning of Chapter 101 of the Texas Civil Practice Remedies Code, its operations are governmental and not proprietary functions. The Corporation is governed by the board of directors appointed and approved by the mayor and City Council.

The Corporation (a) leases all previously existing Department facilities and Department-managed facilities; (b) operates, manages, maintains, develops, and redevelops those existing facilities; (c) has been assigned and now administers all of the Department's obligations and responsibilities, as well as its revenue budgeted as part of the Department's budget, including, but not limited to, municipal HOT receipts, license fees, and concession revenues; and (d) as the City's agent, collects, administers, and audits HOT funds in accordance with terms of City ordinances. The Corporation currently has no employees but has entered into various contracts to provide the personnel and expertise required to operate its facilities. The City has entered into an interlocal agreement with the Corporation (the "Consolidation Interlocal Agreement"), whereby the Corporation will pay $1,380,000 per year to lease all existing Department facilities and Department-managed facilities. The Corporation also agreed to pay the City a one-time fee of $8,620,000 during the City's fiscal year 2012 from operating revenues of the Hotel. The Consolidation Interlocal Agreement's initial term expires on December 31, 2026, but will be extended automatically until June 30, 2041, unless canceled by either party on or before June 30, 2026.

The Corporation is presented as a discretely presented component unit of the City (legally separate from the City). Board members are appointed by the mayor of the City and confirmed by the City Council.

On March 4, 2013, the Corporation formed Houston First Holdings, LLC (HFH), a wholly owned subsidiary of the Corporation, as a “special-purpose” entity for the purpose of owning, holding, selling, leasing, transferring, exchanging, operating, managing, and otherwise dealing with the property known as the Hilton Americas–Houston and its parking garage. The subsidiary is included in the financial statements of the Corporation and all intercompany accounts and transactions are eliminated in consolidation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting — The financial statements of the Corporation have been prepared on the accrual basis of accounting, a flow of economic resources measurement focus. Under the measurement focus, resources are recognized in the period earned, and expenses are recognized in the period incurred.

The Corporation defines operating revenues and expenses consistent with the precepts of Statement of Government Accounting Standards No. 9 paragraphs 16-19 and 31. Generally, receipts collected or due from customers for providing services are considered operating revenues. The payments or amounts due to provide these services are considered operating expenses. All other receipts and payments are considered nonoperating. The significant accounting policies are described below.

Cash and Cash Equivalents — The Corporation defines cash and cash equivalents as cash and investments that are highly liquid, with less than three-month maturities when purchased.

Accounts Receivable — Accounts receivable are stated at the historical carrying amount net of an allowance for uncollectible accounts. An allowance for uncollectible accounts receivable has been established based on historical experience and any specific customer collection issues that have been identified. Uncollectible accounts receivable are written off when a settlement is reached for an amount that is less than the outstanding historical balance or when management has determined that the balance will not be collected. The allowance for doubtful accounts totaled $10,706 at December 31, 2013 and 2012.

Tax Rebates — Mixed beverage, hotel occupancy, and sales taxes are currently collected in the normal course of hotel operations and subsequently remitted to the local and state taxing authorities. As a result of tax rebate agreements with the City; Metropolitan Transit Authority of Harris County, Texas (“Metro”); Harris County, Texas; and the state of Texas, all of the taxes collected, with the exception of Harris County Houston Sports Authority’s 2% HOT and the state of Texas mixed beverage tax, are rebated to the Corporation and have been pledged to the City’s Hotel Occupancy Tax and Special Revenue Bonds, Series 2001, and the City’s Hotel Occupancy Tax and Special Revenue Refunding Bonds Series 2011 and Series 2012. These rebate agreements expired December 2013.

Tax rebates received from these taxing authorities are forwarded to the City and invested in the City’s general investment pool until such funds are applied against future principal and interest payments due to the City from the Corporation. Tax rebates included in equity in pooled investments held by the City totaled $656,767 and $615,246 as of December 31, 2013 and 2012, respectively.

Prepaid Expenses — Prepaid expenses include prepaid insurance, interest, and other miscellaneous prepaid expenses. Prepaid insurance is expensed on a straight-line basis over the period of the coverage.

Investments — The Corporation participates in a City investment pool managed internally by City personnel. The investment funds are administered using a pooling concept, which combines the monies of various City funds for investment purposes (the “City’s Investment Pools”). The Corporation’s pro rata share of participation in the City’s Investment Pools is displayed in the statements of net position as “Equity in pooled investments” held by the City in accordance with the Governmental Accounting Standards Board (GASB or the “Board”) Accounting Standards Codification on Accounting and Financial Reporting for Certain Investments for External Investment Pools and are carried at fair value. The fair value adjustment is included as part of interest income. The Corporation is apportioned interest earnings from the City’s investment pools based upon the Corporation’s relative pro rata share of the applicable investment pool. All of the Corporation’s funds in the City’s investment pools are restricted for debt service.

Property, Plant, and Equipment — Property, plant, and equipment are recorded at original cost for items purchased. Ordinary maintenance and repairs are charged to expense when incurred. Expenditures related to the development of real estate are carried at cost, plus capitalized carrying charges.

Management reviews its long-lived assets for impairment whenever events indicate that the carrying amount of an asset may not be recoverable. If there is an indication of impairment, management prepares an estimate of future undiscounted cash flows (without interest charges) expected to result from the use of the asset and its eventual disposition. If these cash flows are less than the carrying amount of the asset, an impairment loss is recognized to write down the asset to its estimated fair value. Preparation of estimated expected future cash flows is inherently subjective and is based on management’s best estimate of assumptions concerning expected future conditions. No impairment loss was recognized by the Corporation during the years ended December 31, 2013 and 2012.

Depreciation — Depreciation is provided on a straight-line basis over the estimated useful lives of the depreciable assets, ranging from three to 39 years.

Debt Issuance Costs/Notes Payable — Premiums and discounts included in notes payable are amortized as a component of interest expense over the applicable term using the effective interest method. Debt issuance costs are expensed when incurred.

Unearned Revenue — A parcel of land was conveyed to the Corporation by the City for the construction of the Parking Garage, which is attached to the Hotel. The cost of the land was included as unearned revenue at the City’s recorded cost of $3,144,362. In addition, the City made a grant to the Corporation in the amount of $10 million, which provides the City the right to use up to one-half of the spaces available in the Parking Garage and to share in the net income of the parking proceeds in perpetuity. This right was transferred to the Corporation upon formation.

The Corporation recognizes the unearned revenue as garage revenue ratably over the estimated 39-year useful life of the Parking Garage. Amortization of unearned revenue during the years ended December 31, 2013 and 2012, totaled $337,035 for each year, respectively, which is included in garage revenues.

Revenue Recognition — Service and other sales revenues are recognized when services are rendered or when revenue is earned, net of sales tax.

Advertising Expense — Advertising costs are expensed as incurred. Advertising expense for the years ended December 31, 2013 and 2012, amounted to $180,598 and $493,716, respectively, which is included in general and administrative expenses.

Transfers from Primary Government — In the Consolidation Interlocal Agreement, the City assigned to the Corporation the net available pledged revenues to pay for operating expenses, capital expenditures, and for any other lawful purpose, and they are shown as “Transfers from primary government.” The amount transferred from the Department was $67,584,899 and $64,266,743 for 2013 and 2012, respectively, and represents the HOT and parking revenues remaining after debt service and other debt-related expenses that were paid. Also included in 2012 is a transfer of $5,189,523 from the City for initial working capital.

Transfers to Primary Government — In the Consolidation Interlocal Agreement, the Corporation agreed to make certain payments to the City for obligations previously paid directly by the Department. At December 31, 2013 and 2012, those payments totaled $17,189,549 and $14,769,257, respectively.

Income Taxes — The Corporation is exempt from federal income tax under Section 115(1) of the Internal Revenue Code of 1986.

Effective for taxable years beginning on January 1, 2007, the State of Texas enacted the Revised Texas Franchise Tax, which imposes a tax at the entity level. The Corporation is exempt from the Revised Texas Franchise Tax.

Use of Estimates in Financial Statement Preparation — The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires estimates and assumptions that affect the reported amounts of assets and liabilities, as well as disclosures. The Corporation’s financial statements include amounts that are based on management’s best estimates and judgments. Actual results could differ from those estimates.

Reclassifications — Certain reclassifications to December 31, 2012 financial statement line items have been made to conform to the December 31, 2013 presentation.

New Accounting Pronouncements —In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34*. This statement is to improve financial reporting for a governmental financial reporting entity. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2012. The adoption of this statement as of January 1, 2013, did not have any impact on the Corporation’s financial position, results of operations, or cash flows upon adoption.

In March 2012, the GASB issued Statement No. 66, *Technical Corrections — 2012 — an amendment of GASB Statements No. 10 and No. 62*. The objective of this statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, GASB Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. The Corporation adopted this statement as of January 1, 2013, and determined there was no effect upon its financial position, results of operations, or cash flows.

In June 2012, the GASB issued Statement No. 67, *Financial Reporting for Pension Plans — an amendment of GASB Statement No. 25*. The objective of this statement is to improve financial reporting by state and local governmental pension plans. This statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This statement replaces the requirements of GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* and No. 50, *Pension Disclosures,* as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of GASB Statements No. 25 and 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this statement and to define contribution plans that provide postemployment benefits other than pensions. This statement is effective for financial statements for fiscal years beginning after June 15, 2013. The Corporation has determined there will be no effect upon its financial position, results of operations, or cash flows upon adoption.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions — an amendment of GASB Statement No. 27.* The primary objective of this statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. The provisions of this statement are effective for fiscal years beginning after June 15, 2014. The Corporation has determined there will be no effect upon its financial position, results of operations, or cash flows upon adoption.

In January 2013, the GASB issued Statement No. 69, *Government Combinations and Disposals of Government Operations.* This statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this statement, the term *government combinations* includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. The requirements of this statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis. The Corporation has not determined the impact, if any, upon its financial position, results of operations, or cash flows upon adoption.

In April 2013, the GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees.* The objective of this statement is to improve accounting and financial reporting by state and local governments that extend and receive nonexchange financial guarantees. The provisions of this statement are effective for reporting periods beginning after June 15, 2013. The Corporation has not determined the impact, if any, upon its financial position, results of operations, or cash flows upon adoption.

In November 2013, the GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68.* The objective of this statement is to address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions.* The provisions of this statement are required to be applied simultaneously with the provisions of Statement 68. As with Statement 68, the Corporation has determined there will be no effect upon its financial position, results of operations, or cash flows upon adoption.

3. CASH AND CASH EQUIVALENTS

The Corporation’s investment policy requires all deposits to be fully collateralized with depository insurance, obligations of the United States or its agencies, and instrumentalities (excluding those mortgage-backed securities prohibited by the State of Texas Public Funds Investment Act), or in any other manner and amount provided by law for the deposits of the Corporation.

The Corporation’s cash and cash equivalents balance of $60,880,109 and $51,992,515 as of December 31, 2013 and 2012, respectively, are maintained in cash, demand accounts, and money market mutual funds. The accounts that comprise this balance are described below:

	2013	2012
Demand deposit accounts	$ 56,574,552	$ 48,019,298
Cash on hand	93,634	95,900
Money market	4,211,923	3,877,317
Total	$ 60,880,109	$ 51,992,515

The demand deposit accounts are insured by the Federal Deposit Insurance Corporation per the Dodd Frank Act. The money market account is the sweep balance of one of the demand deposit accounts. It is held with a mutual fund managed by Bank of America and invests primarily in direct obligations of the U.S. government or its agencies and is uninsured.

4. EQUITY IN POOLED INVESTMENTS

Short-term Equity in Pooled Investments — As of December 31, 2013 and 2012, the Corporation's pooled investments included $59,638,613 and $41,820,934, respectively, invested in the Texas Short-Term Asset Reserve Program ("TexSTAR"). TexSTAR was created in April 2003, under the Interlocal Cooperation Act of the State of Texas Article 4413 (32C), Vernon's Texas Civil Statutes, as amended. It is administered by First Southwest Asset Management, Inc., and JP Morgan Chase. The fund is rated AAAm by Standard & Poor's. The TexSTAR investment pools' investments are not evidenced by securities that exist in physical or book entry form and, accordingly, do not have custodial risk.

As with all the investment pools, funds are readily available to support daily cash requirements, while maintaining yields slightly higher than standard bank deposit accounts.

Equity in Pooled Investments — Restricted — The City issued bonds in 2001, 2011, and 2012, a portion of which was for the benefit of the Corporation to fund construction, interest, and operating expenses incurred during the construction of the Hotel. In addition, certain proceeds were designated as debt service reserve funds to be used by the Corporation to service the debt during the initial months of the Hotel's operations and during periods of decreased operational liquidity. Also, the Corporation makes monthly payments to the City that provides funding for the semiannual bond payments made by the City. These funds are referred to as the debt service funds. All above-referenced funds are held in the City's Investment Pools. The balance of such accounts at December 31, 2013 and 2012, totaled $34,117,687 and $35,027,021, respectively.

At December 31, 2013 and 2012, the Corporation's exposure to interest rate risk as measured by the segmented time distribution by investment type is summarized below:

	December 31, 2013 Fair Value	Investment Maturities in Years Less than 1	1–5
City of Houston General Pool	$34,117,687	$ -	$34,117,687
City of Houston General Pool	59,638,613	59,638,613	-
Total Investment Pools	$93,756,300	$59,638,613	$34,117,687

	December 31, 2012 Fair Value	Investment Maturities in Years Less than 1	1–5
City of Houston General Pool	$35,027,021	$ -	$35,027,021
TexSTAR	41,820,934	41,820,934	-
Total Investment Pools	$76,847,955	$41,820,934	$35,027,021

The Corporation's exposure to credit risk at December 31, 2013 and 2012, is presented below by investment category as rated by Standard & Poor's and Fitch:

	December 31, 2013 Fair Value	Rating
City of Houston General Pool	$34,117,687	AAA by Fitch
TexSTAR	59,638,613	AAAm by Standard & Poor's
Total Investment Pools	$93,756,300	

	December 31, 2012 Fair Value	Rating
City of Houston General Pool	$35,027,021	AAA by Fitch
TexSTAR	41,820,934	AAAm by Standard & Poor's
Total Investment Pools	$76,847,955	

5. PROPERTY, PLANT, AND EQUIPMENT — NET

The changes in the Corporation's property, plant, and equipment for the years ended December 31, 2013 and 2012, were as follows:

	January 1, 2013	Additions	Retirements	December 31, 2013
Property, plant, and equipment, not subject to depreciation:				
Land	$ 12,997,872	$ 1,820,423	$	$ 14,818,295
Work in process	4,171,224	6,158,202	(8,546,615)	1,782,811
Total property, plant, and equipment, not subject to depreciation	17,169,096	7,978,625	(8,546,615)	16,601,106
Property, plant, and equipment, subject to depreciation:				
Hotel and garage buildings	243,849,412	7,196,856		251,046,268
Furnishings and equipment	42,196,335	1,344,660		43,540,995
Total property, plant, and equipment, subject to depreciation	286,045,747	8,541,516		294,587,263
Less accumulated depreciation for:				
Hotel and garage buildings	(56,628,932)	(7,269,657)		(63,898,589)
Furnishings and equipment	(25,141,094)	(2,266,267)		(27,407,361)
Total accumulated depreciation	(81,770,026)	(9,535,924)		(91,305,950)
Total property, plant, and equipment — net	$ 221,444,817	$ 6,984,217	$ (8,546,615)	$ 219,882,419

	January 1, 2012	Additions	Retirements	December 31, 2012
Property, plant, and equipment, not subject to depreciation:				
Land	$ 12,997,872	$ -	$ -	$ 12,997,872
Work in process	39,754	7,991,387	(3,859,917)	4,171,224
Total property, plant, and equipment, not subject to depreciation	13,037,626	7,991,387	(3,859,917)	17,169,096
Property, plant, and equipment, subject to depreciation:				
Hotel and garage buildings	243,849,412	-	-	243,849,412
Furnishings and equipment	38,336,418	3,859,917	-	42,196,335
Total property, plant, and equipment, subject to depreciation	282,185,830	3,859,917	-	286,045,747
Less accumulated depreciation for:				
Hotel and garage buildings	(50,376,383)	(6,252,549)	-	(56,628,932)
Furnishings and equipment	(22,188,104)	(2,952,990)	-	(25,141,094)
Total accumulated depreciation	(72,564,487)	(9,205,539)	-	(81,770,026)
Total property, plant, and equipment — net	$ 222,658,969	$ 2,645,765	$ (3,859,917)	$ 221,444,817

6. NOTES PAYABLE

The Corporation's notes payable and related premium for the years ended December 31, 2013 and 2012, were as follows:

	January 1, 2013	Payments/ Amortization	Additions	December 31, 2013
Notes payable				
Notes payable — City of Houston	$ 241,530,000	$ (9,875,000)	$ -	$ 231,655,000
Premium — net of discount	5,467,632	(1,326,552)	-	4,141,080
Total notes payable COH	246,997,632	(11,201,552)	-	235,796,080
Note payable — VALIC	-	-	50,000,000	50,000,000
Total notes payable	$ 246,997,632	$ (11,201,552)	$ 50,000,000	$ 285,796,080

	January 1, 2012	Payments/ Amortization	Effect of City's Refunding	December 31, 2012
Notes payable:				
Notes payable — City of Houston	$ 253,970,000	$ (12,720,000)	$ 280,000	$ 241,530,000
Premium — net of discount	4,348,252	(1,424,790)	2,544,170	5,467,632
Total notes payable	$ 258,318,252	$ (14,144,790)	$ 2,824,170	$ 246,997,632

Payment of the Corporation's notes payable to the City is based on the amortization of the City hotel-allocated bonds. The Variable Annuity Life Insurance Company (VALIC) loan requires monthly interest payments only until maturity on May 1, 2020. Scheduled principal and interest payments on debt are summarized as follows:

Years Ending December 31	Principal	Interest	Total
2014	$ 7,840,000	$ 10,109,631	$ 17,949,631
2015	7,835,000	9,717,631	17,552,631
2016	8,310,000	9,325,881	17,635,881
2017	8,710,000	8,910,381	17,620,381
2018	9,115,000	8,485,769	17,600,769
2019–2023	101,875,000	31,614,510	133,489,510
2024–2028	64,445,000	20,104,188	84,549,188
2029–2033	73,525,000	8,236,775	81,761,775
Total	$ 281,655,000	$ 106,504,766	$ 388,159,766

On August 31, 2011, the City issued Hotel Occupancy Tax and Special Revenue Refunding Bonds, Series 2011A and 2011B. The bonds mature in varying amounts from 2012 to 2033. The Series B Bonds were hotel-allocated bonds, and the proceeds were used to refund the hotel-allocated portion of the City's Hotel Occupancy Tax and Special Revenue Bonds, Series 2001A, a portion of the Series 2001B, to convert a portion of the Series 2001C variable-rate debt to fixed-rated debt, and to fund an additional deposit to the debt service reserve fund. The Corporation's notes payable was similarly affected.

On August 15, 2012, the City issued $41,525,000 of Convention & Entertainment Facilities Department Hotel Occupancy Tax (HOT) and Special Revenue Refunding Bonds, Series 2012 with 5% coupons. The true interest cost was 4.8%. The bonds mature in varying amounts from 2026 to 2033. Proceeds were used to refund $41,245,000 of the 2001B2 Convention & Entertainment HOT and Special Revenue Refunding Bonds. Net present value savings totaled $1.9 million or 4.67% of the refunded bonds and reduced total debt service by $1.9 million.

Of the total $231,655,000 notes payable, $156,655,000 of the principal balance relates to the City's fixed-rate bonds and carries interest rates ranging from 1.5% to 5.25%. The remaining $75,000,000 relates to the City's variable rate bonds and is issued as seven-day auction rate securities, with 10% being the maximum interest rate permitted. The variable rate at December 31, 2013 and 2012, was approximately 0.26% and 0.50%, respectively. Fees on the variable-rate bonds are 0.07% and 0.27% per year for 2013 and 2012, respectively. Interest presented on the above payment schedule is calculated on the stated interest rate on the fixed-rate bonds and the interest rate as of December 31, 2013, on the variable-rate bonds, plus expenses, for a total variable rate of 0.33%. The Corporation's allocable portion of the note premiums, net of discounts, is amortized over the term of the note using the effective interest method. Amortization on such amounts totaled $1,326,552 and $1,424,790 for the years ended December 31, 2013 and 2012, respectively.

As of December 31, 2012, the notes payable to the City was secured with a deed of trust and a security interest in certain parcels of land. In connection with the Mortgage Loan described below, the deed of trust was released by the City and utilized to secure the Mortgage Loan.

On April 3, 2013, the Corporation closed a $125,000,000 mortgage loan with VALIC, ("the Mortgage Loan"), which is secured by a deed of trust on the Hilton, its parking garage, the improvements located thereon, and certain personal property. The proceeds will be used to further economic development in and around the Convention Center and the Hilton, including, but not limited to, a new 1,000-room convention center hotel, a new 1,900-space parking garage, and certain other residential and retail opportunities to be located on the north end of the Convention Center.

The initial loan advance of $50,000,000 was funded on April 4, 2013, at an initial interest rate ("Initial Interest Rate") of 3.9%. Each subsequent advance shall bear interest at the greater of the (i) Initial Interest Rate or (ii) 270 basis points, plus the semiannual yield on the Treasury Constant Maturity Series with maturity equal to seven years.

In consideration of the Mortgage Loan, VALIC required the Corporation to pay certain reserves to be held with their agent. The reserves represent the subordinated management fee and the deferred fee from Hotel Operator as discussed in Note 8, and a reserve for furniture, fixtures, and equipment replacement and renewal. As of December 31, 2013, the deposits held by others included in the statements of net position totaled $12,812,544.

7. SUMMARY OF CASH FLOWS FROM OPERATIONS APPLICATION PRIORITY

Cash flows from hotel operations shall be applied to the following items in the following order of priority:

- First, to the payment of the note payable due to the City pursuant to the amortization schedule after taking into account all credits for tax rebates;

- Second, an amount equal to the excess of the preferred return over the current-year note payment shall be applied first to expenses of the Department and then to the corporate reserve fund, up to its defined maximum amount;
- Third, to the primary capital replacement reserve;
- Fourth, to the subordinated portion of the management fee;
- Fifth, to the secondary capital replacement reserve; and
- Sixth, unless otherwise directed by the president of the Corporation, to the City for deposit into the Convention and Entertainment Development Fund.

8. COMMITMENTS AND CONTINGENCIES

Hotel Management Agreement — The Corporation entered into a hotel management agreement (the "Management Agreement") on March 21, 2001, with the Hilton Hotels Corporation (the "Hotel Operator") for the Hilton. The Management Agreement has a term of 15 years and commenced with the opening of the Hotel. Under the terms of the Management Agreement, the Hotel Operator has agreed to manage, operate, and market the Hotel on behalf of the Corporation. For providing such services, the Hotel Operator will receive a management fee consisting of a base management fee and a subordinated management fee. The management fee is adjusted annually based on the percent change in the competitive set's prior 12-month revenue per available room. During 2013 and 2012, the base management fee expense increased $271,071 and $231,780 for a total of $2,530,139 and $2,259,068, respectively.

The payment of the subordinated management fee is contingent on first generating sufficient operating cash flow (as defined) to fund certain reserves and to provide for a cumulative preferred return to the City, as discussed below. Upon termination or expiration of the Management Agreement, the accrued and unpaid subordinated management fees will be due and payable. The subordinated management fee expense totaled $1,351,751 and $1,236,750 for the years ended December 31, 2013 and 2012, respectively. The cumulative accrued subordinated management fee of $9,441,742 and $8,089,991 is included in long-term liabilities at December 31, 2013 and 2012, respectively.

During 2003, under the terms of the Management Agreement, the Hotel Operator paid the Corporation an inducement fee of $6 million, which was used as a source of funds for project costs. The fee is in the form of an interest-free, self-amortizing loan, the principal balance of which reduces, without payment, 1/180th per month coterminous with the Management Agreement. For the years ended December 31, 2013 and 2012, amortization of the deferred fee totaled $400,000 for each year and was recorded as a reduction of the management fee. In the event the Management Agreement with the Hotel Operator is terminated prior to its expiration date, the unamortized portion of the inducement fee will be payable to the Hotel Operator. At December 31, 2013 and 2012, the deferred inducement fee from the Hotel Operator totaled $1,966,667 and $2,366,667, respectively.

Preferred Return — In accordance with the Consolidation Interlocal Agreement and the Management Agreement, after meeting certain other funding and reserve requirements, the City can require the distribution of a preferred return from available cash flow (as defined) equal to the preferred return amount of $25 million per year, less the debt service for the applicable year. The preferred return is paid in the subsequent year and recorded as a distribution of net position when paid. In conjunction with the Consolidation, the preferred return payments are retained by the Corporation since the Department venues' operations were moved to the Corporation.

Development & Funding Agreement – On April 9, 2013, the Corporation entered into a Development and Funding Agreement with Houston Convention Center Hotel, LLC ("Hotel Owner"), for the development of an approximately 1,000-room hotel facility located on the north end of the Convention

Center. In accordance with the Development & Funding Agreement, the Corporation is obligated to a) design, construct, operate, and maintain a parking garage and skybridges; b) purchase the hotel site land; c) convey the hotel site land to the Hotel Owner; and d) subject to certain benchmarks, loan $27 million to the Hotel Owner. The Hotel Owner is obligated to a) design, construct, operate, and maintain the hotel facility and b) reimburse the Corporation a total of $62 million for the hotel site land and the loan commencing on January 5 following the year in which the hotel facility opens.

In accordance with the Development & Funding Agreement, in April 2013, the Corporation loaned $31,897,494 to Houston First Foundation (HFF), a Texas nonprofit and related party, to enable HFF to purchase the hotel site land. The loan to HFF earns interest at the same rate as the Mortgage Loan discussed in Note 6. Interest earned as of December 31, 2013, was $922,635. The total amount due of $32,820,129 is reflected on the statements of net position as due from affiliates.

As of December 31, 2013, $1,030,855 is included in Property, plant and equipment - work in progress for the development of the parking garage and skybridges. No funds have been advanced to the Hotel Owner and title to the hotel site land remains with HFF as of December 31, 2013.

9. RISK MANAGEMENT

As the owner of the Hotel operated as the Hilton, and as a local government corporation, the Corporation maintains, or has maintained on its behalf, various policies and/or insurance programs to cover the various risks of loss it is exposed to. Through commercial policies, the following coverages have been secured: property, general liability, umbrella liability, auto, and theft. In lieu of a workers' compensation policy, the Hilton has procured a nonsubscriber program administered by a third-party administrator. Due to the division of responsibilities, the Corporation maintains separate policies for directors and officers, employment practices liability, crime, and property.

10. SUBSEQUENT EVENTS

The Corporation has evaluated subsequent events for potential recognition and/or disclosures through October 23, 2014, the date the financial statements were available to be issued and noted no matters other than the following.

A. The Corporation received the balance of the Mortgage Loan discussed in Note 6. On March 13, 2014, the Corporation received $30 million bearing interest at a rate of 4.78%. On July 29, 2014, the Corporation received $45 million bearing interest at a rate of 4.81%.

B. On April 14, 2014, in accordance with the Development and Funding Agreement discussed in Note 8, the Corporation transferred $27 million to an escrow account to fund its required obligation to the Hotel Owner. In addition, on this date, HFF transferred the hotel site land to the Hotel Owner. As a result, the Corporation transferred $1,431,129 to HFF and swapped HFFs' portion of the loan to the Hotel Owner for the receivable. The total loan from the Hotel Owner to the Corporation amounted to $58,700,000 resulting in scheduled principal and interest payments on the loan as follows with anticipated opening to occur during fiscal year 2016:

Years Ending December 31	Principal	Interest	Total
2017	$ 152,851	$ 97,149	$ 250,000
2018	153,104	96,896	250,000
2019	153,358	96,642	250,000
2020	153,612	96,388	250,000
2021	153,866	96,134	250,000
2022–2026	773,158	476,842	1,250,000
2027–2031	2,033,721	466,279	2,500,000
2032–2036	3,553,090	446,910	4,000,000
2037–2041	7,096,683	403,317	7,500,000
2042–2046	7,155,602	344,398	7,500,000
2047–2051	7,715,011	284,989	8,000,000
2052–2056	9,787,353	212,647	10,000,000
2057–2061	9,868,612	131,388	10,000,000
2062–2066	9,949,979	50,021	10,000,000
Total	$ 58,700,000	$ 3,300,000	$ 62,000,000

C. On June 18, 2014, the Corporation entered into a Services Agreement with the Greater Houston Convention and Visitors Bureau ("the Bureau") which engaged the Corporation to provide advertising and promotional programs on behalf of the Bureau at the same levels as previously funded by the Corporation to the Bureau. The Bureau's employees have been added to the Corporation's existing personnel contracts effective July 1, 2014. The Services Agreement required the Corporation to amend the Certificate of Formation to increase the number of authorized board members from 11 to 13.

D. On July 23, 2014, the City issued $73,725,000 of Convention & Entertainment Facilities Department Hotel Occupancy Tax (HOT) and Special Revenue Refunding Bonds, Series 2014. This issue included $52,195,000 of Serial Bonds with stated interest rates between 2% and 5% maturing in various amounts from 2015 to 2032, and $21,530,000 of Term Bonds with stated interest rates of 5% maturing in various amounts from 2033 to 2039. The true interest cost was 4%. Proceeds were used to (a) refund the City's Outstanding Convention & Entertainment Facilities Department Hotel Occupancy Tax and Special Revenue Refunding Bonds, Series 2012; (b) finance certain project costs; and (c) pay the costs of issuance of the Bonds. Net present value savings totaled $4.6 million or 11% of the refunded bonds.

E. On October 1, 2014, the Corporation executed a Management Agreement Termination Agreement (the "Termination Agreement") to terminate the Management Agreement as described in Note 8 and executed a new Management Agreement (the "New Management Agreement") with the Hotel Operator for the Hilton both with an effective date of January 1, 2014. In connection with the Termination Agreement, the Hotel Operator released the Corporation from repayment of the unamortized inducement fee and the Corporation disbursed the accrued subordinated management fee as discussed in Note 8. The New Management Agreement is for 15 years and consistent with the original Management Agreement, the New Management Agreement also provides for a base management fee of $1,900,000 and a subordinated management fee subject of $850,000 (collectively referred to as the "Management Fees"). The Management Fees adjust annually based on the percentage change in the competitive set's prior 12-month revenue per available room with the base fee to commence adjustment effective January 1, 2015 and the subordinate fee to commence adjustment effective January 1, 2017. The subordinate fee is also subject to sufficient operating cash flows (as defined) and any unpaid subordinated fees will accrue. Upon termination of the New Management Agreement, any unpaid subordinated fees will be due and payable.

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