Houston First Corporation

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

Financial Statements as of and for the Years
Ended December 31, 2014 and 2013, and
Independent Auditors' Report

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

TABLE OF CONTENTS

Deloitte & Touche LLP
Suite 4500
1111 Bagby Street
Houston, TX 77002
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 consolidated financial statements of Houston First Corporation and its subsidiary (the "Corporation"), which comprise the statements of net position as of December 31, 2014 and 2013, 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 consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the net position of Houston First Corporation and its subsidiary as of December 31, 2014 and 2013, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3-9 be presented to supplement the basic consolidated financial statements. Such information, although not a part of the basic consolidated financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic 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 basic financial statements, and other knowledge we obtained during our audit of the basic 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

September 10, 2015

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, 2014 and 2013, 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.

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 a minimum of 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 contract effective July 1, 2014. The Services Agreement required the Corporation to amend its Certificate of Formation to increase the number of authorized board members from 11 to 13 to include 2 Bureau board members.

For the years ended December 31, 2014 and 2013, 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 14–25 of this report.

NET POSITION

Total net position at December 31, 2014, was $135,442,004, a 38.4% increase from December 31, 2013. Total net position at December 31, 2013, was $97,873,970, a 57.5% increase from December 31, 2012.

CONDENSED STATEMENTS OF NET POSITION

DECEMBER 31, 2014, 2013 AND 2012

	2014	2013	2012
Current assets	$ 261,280,270	$ 129,017,360	$ 100,932,626
Noncurrent assets	69,948,207	85,783,395	43,336,921
Capital assets	238,844,374	219,882,419	221,444,817
Total assets	$ 570,072,851	$ 434,683,174	$ 365,714,364
Deferred outflow of resources	$ 393,569	$ 1,580,743	$ 1,661,106
Current liabilities	$ 43,898,337	$ 40,016,562	$ 48,321,447
Long-term liabilities	391,126,079	298,373,385	256,925,221
Total liabilities	$ 435,024,416	$ 338,389,947	$ 305,246,668
Net position	$ 135,442,004	$ 97,873,970	$ 62,128,802

Total assets increased $135,389,677 to $570,072,851 at December 31, 2014, from $434,683,174 at December 31, 2013. This increase is primarily the result of the final draws on the new mortgage loan with The Variable Annuity Life Insurance Company (VALIC) totaling $75,000,000 combined with $39,200,000 in new money proceeds from the 2014 refunding, both more fully described in Note 8. These proceeds resulted in an increase in short-term equity in pooled investments and net property, plant, and equipment which increased $18,961,955.

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 8. 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.

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, 2014 and 2013, 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.

In August 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 entirely; (b) finance certain Convention District 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. Proceeds from the refunding totaled $39,200,000 which were borrowed by the Corporation.

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 $30,025,944 and $34,117,687 at December 31, 2014 and 2013, respectively.

The Corporation made principal payments totaling $7,840,000 and $9,875,000 in 2014 and 2013, respectively. The total notes payable balance includes the Corporation's allocable portion of the unamortized bond premiums, net of discounts, which totaled $10,803,511 and $4,141,080 at December 31, 2014 and 2013, respectively. The net amortization on the premiums and discounts totaled $1,174,137 and $1,326,552 for the years ended December 31, 2014 and 2013, respectively. Accumulated amortization of the bond premiums, net of discounts, totaled $4,323,204 and $3,266,515 at December 31, 2014 and 2013, 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 new money proceeds issued from the Series 2014 refunding of $39,200,000 was borrowed from the City.

Total liabilities increased $96,634,469 to $435,024,416 in 2014 from $338,389,947 in 2013, which was primarily attributable to the remaining draws of $75 million on the mortgage loan and the $32,200,000 net increase in principal and $7,836,568 net increase in premium from the Series 2014 refunding, offset by the principal payment on the hotel allocated bonds of $7,840,000 and a decrease in the subordinated management fee liability of $8,591,742. The decrease in the subordinated management fee was the result of the termination of the management agreement with the Hilton.

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.

The Corporation's net position increased $37,568,034 to $135,442,004 at December 31, 2014, from $97,873,970 at December 31, 2013. Of this increase, $135,389,677 is attributable to an increase in assets offset primarily by an increase of $96,634,469 liabilities as described above.

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.

CONDENSED STATEMENTS OF CHANGES IN NET POSITION
DECEMBER 31, 2014, 2013, AND 2012

	December 31, 2014	December 31, 2013	December 31, 2012
OPERATING REVENUES:			
Hotel revenues	$ 92,728,856	$ 88,910,489	$ 82,296,639
Venue revenues	18,495,043	19,018,928	16,711,814
Parking revenues	6,211,089	5,583,320	4,704,900
Other operating revenues	5,348,294	3,584,231	3,552,799
Total operating revenues	122,783,282	117,096,968	107,266,152
OPERATING EXPENSES:			
Hotel expenses:			
Direct expenses	30,583,577	30,390,051	28,781,196
Management fees	2,749,237	3,881,890	3,525,818
Depreciation	8,988,382	9,057,292	8,990,539
General and administrative	20,998,284	21,731,301	22,284,187
Lease expense	1,671,583	1,671,583	1,650,215
Other hotel expenses	991,032	1,939,441	3,678,566
Parking expenses	4,535,580	4,683,492	2,107,454
Venue expenses:			
Direct expenses	30,203,382	30,516,372	28,985,037
Depreciation and amortization	751,493	478,632	215,000
General and administrative	11,289,388	7,898,581	8,945,209
Destination marketing expenses	7,740,039	-	-
Total operating expenses	120,501,977	112,248,635	109,163,221
OPERATING INCOME (LOSS)	2,281,305	4,848,333	(1,897,069)
NONOPERATING REVENUES (EXPENSES):			
Other income	-	-	110,668
Tax rebates	521,330	10,317,165	9,799,524
Transfers from primary government	79,695,847	67,584,899	64,266,743
GHCVB contract expense	(9,351,707)	(17,602,125)	(15,610,063)
Sponsorship expense	(4,418,156)	(2,900,531)	(3,091,807)
Transfers to primary government	(18,831,423)	(17,189,549)	(14,769,257)
Transfers to affiliate	(1,471,650)		
Interest expense	(11,708,479)	(9,921,021)	(8,368,772)
Interest income	850,967	607,997	503,476
Total nonoperating revenues (expenses)	35,286,729	30,896,835	32,840,512
CHANGE IN NET POSITION	37,568,034	35,745,168	30,943,443
NET POSITION — Beginning of year	97,873,970	62,128,802	31,185,359
NET POSITION — End of year	$ 135,442,004	$ 97,873,970	$ 62,128,802

1. <u>Operating Revenues</u>

Total operating revenues for 2014 and 2013 were $122,783,282 and $117,096,968, respectively, resulting in an increase of $5,686,314. The majority of the increase in operating revenues for 2014 was attributable to an increase in room revenue at the Hotel. The remaining increase was from an increase in other operating income, resulting from the release of the unearned inducement fee in the Termination Agreement as discussed in Note 10.

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.

2. Tax Rebates

Tax rebates decreased $9,795,835 from $10,317,165 in 2013 to $521,330 in 2014 and increased $517,641 from $9,799,524 in 2012 to $10,317,165 in 2013. The decrease in 2014 was due to the expiration of these rebates in December of 2013. The increase in 2013 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, the remaining initial working capital transfer, and the transfer of other remaining Department fund balances. For 2014, the amount transferred from the Department was $79,695,847, an increase of $12,110,948 from 2013. For 2013, the amount transferred from the Department was $67,584,899, an increase of $3,318,156 from 2012. The increase for both years is from the increase in HOT revenues and parking revenues at the City.

4. Operating Expenses

Total operating expenses increased $8,253,342 from $112,248,635 in 2013 to $120,501,977 in 2014. The increase in 2014 is primarily due to an increase in destination marketing expenses.

Destination marketing expenses increased $7,740,039 in 2014 from $-0- in 2013 and represent the expenses of the operations of the former Greater Houston Convention and Visitors Bureau, which the Corporation assumed on July 1, 2014.

Total operating expenses increased $3,085,414 from $109,163,221 in 2012 to $112,248,635 in 2013. The increase in 2013 is primarily due to an increase in direct operating expenses and management fees.

There was not a significant change in direct operating expenses related to hotel, parking and leased venue operations from 2013 to 2014. 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 operations as a percentage of hotel operating revenues were 34% and 35% in 2013 and 2012, respectively.

Management fees decreased $1,132,653 from $3,881,890 in 2013 to $2,749,237 in 2014. This decrease is the result of the termination of the Management Fee Agreement and executing a New Management Fee Agreement with the Hotel Operator as discussed in Note 10. Management fees increased $356,072 from $3,525,818 in 2012 to $3,881,890 in 2013. The increase is based on the formula provided in the management fee rider of the Management Agreement.

The Corporation's operating income before depreciation totaled $12,021,181 and $14,384,257 in 2014 and 2013, respectively. The Corporation's depreciation expense for 2014 and 2013 totaled $9,739,875 and $9,535,924, respectively.

The Corporation's operating income, which includes the noncash charge of depreciation, totaled $2,281,305 and $4,848,333 in 2014 and 2013, respectively.

5. General and Administrative Expenses

In 2014 and 2013, general and administrative expenses were incurred from both hotel and leased venue operations. General and administrative expenses increased $2,657,790 to $32,287,672 in 2014 from $29,629,882 in 2013. The majority of the increase is attributable to personnel, convention services agreements, and consulting.

Personnel costs increased $924,618 due to a combination of budgeted headcount increases and market adjustments, and an increase in compensated absence accruals. Contractual payments for convention services agreements increased by $713,907. Consulting expenses increased $614,123 for transition consulting, information technology, diversity community outreach and a tourism study.

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.

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, 2014 and 2013, those payments totaled $18,831,423 and $17,189,549, respectively. As one of these payments is based on HOT revenues, the increase of $1,641,874 in 2014 and the increase of $2,420,292 in 2013 were directly related to the increase in HOT revenues for those respective years.

7. Interest Expense

Interest expense increased $1,787,458 from $9,921,021 in 2013 to $11,708,479 in 2014. The increase in interest expense was primarily due to the total new borrowings of $107.2 million offset by capitalization of interest costs on construction of $724,825. In addition, the Corporation incurred $957,433 of bond issue costs for the 2014 refunding included in 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.

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

GHCVB contract expense decreased $8,250,418 from $17,602,125 in 2013 to $9,351,707 in 2014 due to the Services Agreement effective July 1, 2014 as discussed previously.

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.

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

STATEMENTS OF NET POSITION
DECEMBER 31, 2014 AND 2013

	2014	2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 69,434,603	$ 60,880,109
Accounts receivable — net	3,929,085	3,573,007
Due from City of Houston	7,149,170	-
Tax rebates receivable	-	1,479,321
Prepaid expenses and other assets	1,725,985	1,460,818
Deposits held by others — current	3,812,463	1,985,492
Short-term equity in pooled investments	175,228,964	59,638,613
Total current assets	261,280,270	129,017,360
NON-CURRENT ASSETS:		
Due from affiliate	-	32,820,129
Notes receivable	32,153,221	
Deposits held by others — restricted	-	10,827,052
Equity in pooled investments — restricted	30,025,944	34,117,687
Property, plant, and equipment — net	238,844,374	219,882,419
Other assets — net	7,769,042	8,018,527
Total non-current assets	308,792,581	305,665,814
TOTAL ASSETS	570,072,851	434,683,174
DEFERRED OUTFLOW OF RESOURCES — Deferred amounts from debt refunding	393,569	1,580,743
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	18,359,749	14,326,779
Accrued interest	3,113,127	2,646,441
Accrued expenses	11,474,132	9,507,924
Due to City of Houston	-	4,958,383
Subordinated management fee	850,000	-
Current portion of notes payable	9,764,294	7,840,000
Current portion of unearned revenue	337,035	337,035
Current portion of inducement fee from Hotel Operator	-	400,000
Total current liabilities	43,898,337	40,016,562
LONG-TERM LIABILITIES:		
Notes payable	382,054,217	277,956,080
Unearned revenue	9,071,862	9,408,896
Inducement fee from Hotel Operator	-	1,566,667
Subordinated management fee	-	9,441,742
Total long-term liabilities	391,126,079	298,373,385
Total liabilities	435,024,416	338,389,947
COMMITMENTS AND CONTINGENCIES (Notes 8 and 10)		
NET POSITION		
Net investment in capital assets	3,000,796	2,589,944
Restricted for debt service	9,295,838	14,996,850
Unrestricted	123,145,370	80,287,176
TOTAL NET POSITION	$ 135,442,004	$ 97,873,970

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, 2014 AND 2013

	2014	2013
OPERATING REVENUES:		
Hotel revenues	$ 92,728,856	$ 88,910,489
Venue revenues	18,495,043	19,018,928
Parking revenues	6,211,089	5,583,320
Other operating revenues	5,348,294	3,584,231
Total operating revenues	122,783,282	117,096,968
OPERATING EXPENSES:		
Hotel expenses:		
Direct expenses	30,583,577	30,390,051
Management fees	2,749,237	3,881,890
Depreciation and amortization	8,988,382	9,057,292
General and administrative	20,998,284	21,731,301
Lease expense	1,671,583	1,671,583
Other hotel expenses	991,032	1,939,441
Parking expenses	4,535,580	4,683,492
Venue expenses:		
Direct expenses	30,203,382	30,516,372
Depreciation and amortization	751,493	478,632
General and administrative	11,289,388	7,898,581
Destination marketing expenses	7,740,039	-
Total operating costs and expenses	120,501,977	112,248,635
OPERATING INCOME	2,281,305	4,848,333
NONOPERATING REVENUES (EXPENSES):		
Tax rebates	521,330	10,317,165
Transfers from primary government	79,695,847	67,584,899
GHCVB contract expense	(9,351,707)	(17,602,125)
Sponsorship expense	(4,418,156)	(2,900,531)
Transfers to primary government	(18,831,423)	(17,189,549)
Transfers to affiliate	(1,471,650)	-
Interest expense	(11,708,479)	(9,921,021)
Interest income	850,967	607,997
Total nonoperating revenues (expenses)	35,286,729	30,896,835
INCREASE IN NET POSITION	37,568,034	35,745,168
NET POSITION — Beginning of year	97,873,970	62,128,802
NET POSITION — End of year	$ 135,442,004	$ 97,873,970

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, 2014 AND 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from customers	$ 123,244,366	$ 117,192,091
Cash payments to suppliers for goods and services	(73,523,621)	(62,034,724)
Cash payments to employees for services	(42,359,675)	(38,328,124)
Cash transfers from the City per agreements	67,588,294	60,246,230
Cash payments to the City per agreements	(20,051,884)	(18,070,904)
Cash payments to GHCVB	(13,636,405)	(16,362,356)
Cash payments to affiliate	(1,471,650)	-
Cash payments for sponsorships	(4,418,156)	(2,900,531)
Net cash provided by operating activities	35,371,269	39,741,682
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:		
Proceeds from debt financing	27,000,000	31,897,494
Payments for interest	(1,631,025)	(1,231,795)
Net cash provided by non-capital financing activities	25,368,975	30,665,699
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Payments for interest	(9,770,453)	(9,085,272)
Receipt of tax rebates	2,000,656	9,682,215
Principal payment on note payable	(7,840,000)	(9,875,000)
Proceeds from debt financing	89,166,721	6,444,135
Payment for debt issuance costs	(957,433)	(166,250)
Receipt (payment) for deposits held by others	9,000,081	(1,420,414)
Acquisition of property, plant, and equipment	(23,804,589)	(7,978,724)
Net cash provided by (used in) capital and related financing activities	57,794,983	(12,399,310)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments from (loans to)affiliates	32,820,129	(31,897,494)
Loans to others	(32,153,221)	-
Interest received (paid) on investments	429,468	(193,385)
Purchase of investments	(209,959,218)	(66,999,414)
Proceeds from sales and maturities of investments	98,882,109	49,969,816
Net cash used in investing activities	(109,980,733)	(49,120,477)
NET INCREASE IN CASH AND CASH EQUIVALENTS	8,554,494	8,887,594
CASH AND CASH EQUIVALENTS — Beginning of year	60,880,109	51,992,515
CASH AND CASH EQUIVALENTS — End of year	$ 69,434,603	$ 60,880,109

(Continued)

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

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	$ 2,281,305	$ 4,848,333
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	9,739,875	9,535,924
Amortization of Hotel Operator fee	(1,966,667)	(400,000)
(Decrease) increase in subordinated management fee	(9,441,742)	1,351,751
(Increase) decrease in accounts receivable — net	(356,078)	330,470
Increase in prepaid expenses and other assets	(265,168)	(113,830)
Increase in deposits held by others	-	(702,504)
Decrease in other assets	249,485	291,373
(Decrease) increase in accounts payable	(864,270)	1,808,987
Increase in accrued expenses	2,816,206	874,188
Decrease in due to primary government	(10,701,234)	(7,338,669)
Decrease in current portion of unearned revenue	(337,034)	(637,035)
Nonoperating income (expenses):		
Transfers from City	78,289,528	67,584,899
Other City obligations	(18,831,423)	(17,189,549)
GHCVB contract expense	(9,351,708)	(17,602,125)
Sponsorship expense	(5,889,806)	(2,900,531)
Net cash provided by operating activities	$ 35,371,269	$ 39,741,682
NONCASH TRANSACTIONS:		
Capital additions included in liabilities	$ 6,399,064	$ 929,048
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.

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 a minimum of 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. The expenses incurred as a result of the Services Agreement are included in operating expenses as destination marketing expenses.

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, 2014 and 2013, respectively.

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 $110,123 and $656,767 as of December 31, 2014 and 2013, 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, 2014 and 2013.

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 straight-line 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 Hilton 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, 2014 and 2013 totaled $337,035 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, 2014 and 2013, amounted to $1,487,019 and $180,598, 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 $79,695,847 and $67,584,899 for 2014 and 2013, respectively, and represents the HOT and parking revenues remaining after debt service and other debt-related expenses were paid.

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, 2014 and 2013, those payments totaled $18,831,423 and $17,189,549, 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.

New Accounting Pronouncements —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. Upon adoption, the Corporation has determined there is no impact upon its financial position, results of operations, or cash flows; however, the statement requires disclosure. Note 1 gives the date, a brief description of the transfer, and the reason for the transfer of operations.

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 determined there will be no effect upon its financial position, results of operations, or cash flows upon adoption.

In February 2015, the GASB issued Statement No. 72, *Fair Value Measurement and Application.* The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2015. The Corporation has not yet determined the effect upon its financial position, results of operations, or cash flows upon adoption.

In August 2015, the GASB issued Statement No. 77, *Tax Abatement Disclosure*. Tax abatements are widely used by state and local governments, particularly to encourage economic development. For financial reporting purposes, this Statement defines a tax abatement as resulting from an agreement between a government and an individual or entity. In the agreement the government promises to forgo tax revenues and the individual or entity promises to subsequently take a specific action that contributes to economic development or otherwise benefits the government or its citizens. This Statement requires disclosure of tax abatement information about (1) a reporting government's own tax abatement agreements and (2) those that are entered into by other governments and that reduce the reporting government's tax revenues. The provisions of this statement are effective for reporting periods beginning after December 15, 2015. The Corporation has not yet determined the 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 $69,434,603 and $60,880,109 as of December 31, 2014 and 2013, respectively, are maintained in cash, demand accounts, and money market mutual funds. The accounts that comprise this balance are described below:

	2014	2013
Demand deposit accounts	$ 65,729,619	$ 56,574,552
Cash on hand	100,793	93,634
Money market	3,604,191	4,211,923
Total	$ 69,434,603	$ 60,880,109

The demand deposit accounts are either fully collateralized by the depository institution primarily in direct obligations of the U.S. government or its agencies, or insured by the Federal Deposit Insurance Corporation. 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, 2014 and 2013, the Corporation's pooled investments included $175,228,964 and $59,638,613, 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, 2012, and 2014, 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, the Convention District Projects, and the Development and Funding Agreement discussed in Note 8. 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. In addition, the Corporation makes monthly payments to the City to fund the semiannual bond payments made by the City. These funds are designated as debt service funds. All above-referenced funds are held in the City's Investment

Pools. The balance of such accounts at December 31, 2014 and 2013, totaled $30,025,944 and $34,117,687, respectively.

At December 31, 2014 and 2013, the Corporation's exposure to interest rate risk as measured by the segmented time distribution by investment type is summarized below:

	December 31, 2014 Fair Value	Investment Maturities in Years	
		Less than 1	1–5
City of Houston General Pool	$ 30,025,944	$ -	$ 30,025,944
TexSTAR	175,228,964	175,228,964	-
Total Investment Pools	$ 205,254,908	$ 175,228,964	$ 30,025,944

	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
TexSTAR	59,638,613	59,638,613	-
Total Investment Pools	$ 93,756,300	$ 59,638,613	$ 34,117,687

The Corporation's exposure to credit risk at December 31, 2014 and 2013 is presented below by investment category as rated by Standard & Poor's and Fitch:

	December 31, 2014 Fair Value	Rating
City of Houston General Pool	$ 30,025,944	AAA by Fitch
TexSTAR	175,228,964	AAAm by Standard & Poor's
Total Investment Pools	$ 205,254,908	

	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	

5. DEPOSITS HELD BY OTHERS

As discussed in Note 8, 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. In consideration of the Mortgage Loan, VALIC required the Corporation to fund 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 10, and a reserve for furniture, fixtures, and equipment replacement and renewal. As more fully described in Note 10, the termination of the former Hotel Management Agreement in 2014 caused a corresponding release of the subordinated management fee reserves. As of December 31, 2014 and 2013, the deposits held by others included in the statements of net position totaled $3,812,463 and $12,812,544, respectfully.

6. NOTES RECEIVABLE AND DUE FROM AFFILIATE

As more fully described in Note 10, 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. In accordance with this agreement, in April 2013, the Corporation loaned funds to Houston First Foundation ("HFF"), a Texas nonprofit and related party, to enable HFF to purchase the hotel site land. The loan to HFF earned interest at the same rate as the Mortgage Loan discussed in Note 8. Interest earned as of December 31, 2014 and 2013, was $414,667 and $922,635, respectively. The total amount due of $32,820,129 is reflected on the statements of net position as due from affiliate on December 31, 2013.

On April 14, 2014, HFF sold the hotel site land to the Hotel Owner. As a result, the Corporation swapped HFF's portion of the loan to the Hotel Owner for the receivable from HFF and transferred $1,471,650 to HFF. The Corporation also transferred $27 million to an escrow account to fund its required obligation to the Hotel Owner. As of December 31, 2014, the amount of the receivable from the Hotel Owner totaled $32,153,221, and no funds have been advanced to the Hotel Owner from the escrow. Once the escrow account is fully disbursed, the total loan from the Hotel Owner to the Corporation will be $59,153,221.

Based on an anticipated opening of the new hotel to occur during fiscal year 2016, the scheduled payments on the loan are as follows:

Years Ending December 31		**Total Payments**
2016	$	-
2017		250,000
2018		250,000
2019		250,000
2020		250,000
2021–2025		1,250,000
2026–2030		2,250,000
2031–2035		3,500,000
2036–2040		7,000,000
2041–2045		7,500,000
2046–2050		7,500,000
2051–2055		10,000,000
2056–2060		10,000,000
2061–2064		9,153,221
Total	$	59,153,221

7. PROPERTY, PLANT, AND EQUIPMENT — NET

The changes in the Corporation's property, plant, and equipment for the years ended December 31, 2014 and 2013, were as follows:

	January 1, 2014	Additions/ Transfers	Retirements/ Transfers	December 31, 2014
Property, plant, and equipment, not subject to depreciation:				
Land	$ 14,818,295	$ 6,003	-	$ 14,824,298
Construction in progress	1,782,811	28,675,018	(7,523,711)	22,934,118
Total property, plant, and equipment, not subject to depreciation	16,601,106	28,681,021	(7,523,711)	37,758,416
Property, plant, and equipment, subject to depreciation:				
Hotel and garage buildings	251,046,268	5,441,139	-	256,487,407
Furnishings and equipment	43,540,995	2,103,381	(182,992)	45,461,384
Total property, plant, and equipment, subject to depreciation	294,587,263	7,544,520	(182,992)	301,948,791
Less accumulated depreciation for:				
Hotel and garage buildings	(63,898,589)	(7,637,608)	-	(71,536,197)
Furnishings and equipment	(27,407,361)	(2,102,267)	182,992	(29,326,636)
Total accumulated depreciation	(91,305,950)	(9,739,875)	182,992	(100,862,833)
Total property, plant, and equipment — net	$ 219,882,419	$ 26,485,666	$ (7,523,711)	$ 238,844,374

	January 1, 2013	Additions/ Transfers	Retirements/ Transfers	December 31, 2013
Property, plant, and equipment, not subject to depreciation:				
Land	$ 12,997,872	$ 1,820,423	$ -	$ 14,818,295
Construction in progress	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

8. NOTES PAYABLE

The Corporation's notes payable and related premium for the years ended December 31, 2014 and 2013 were as follows:

	January 1, 2014	Payments/ Amortization	Additions	December 31, 2014
Notes payable				
Notes payable — City of Houston	$ 231,655,000	$ (7,840,000)	$ 32,200,000	$ 256,015,000
Premium — net of discount	4,141,080	(2,304,290)	8,966,721	10,803,511
Total notes payable COH	235,796,080	(10,144,290)	41,166,721	266,818,511
Note payable — VALIC	50,000,000	-	75,000,000	125,000,000
Total notes payable	$ 285,796,080	$ (10,144,290)	$ 116,166,721	$ 391,818,511

	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

Payment of the Corporation's notes payable to the City is based on the amortization of the City hotel-allocated bonds and HFC-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
2015	$ 8,590,000	$ 14,933,090	$ 23,523,090
2016	9,085,000	14,414,781	23,499,781
2017	9,520,000	13,968,281	23,488,281
2018	9,960,000	13,511,269	23,471,269
2019	10,470,000	13,244,129	23,714,129
2020–2024	184,335,000	35,735,070	220,070,070
2025–2029	71,475,000	22,930,700	94,405,700
2030–2034	66,605,000	9,465,688	76,070,688
2034–2039	10,975,000	1,701,000	12,676,000
Total	$ 381,015,000	$139,904,008	$ 520,919,008

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.

In August 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.

Of the total $256,015,000 notes payable, $181,015,000 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, 2014 and 2013 was approximately 0.17% and 0.26%, respectively. Fees on the variable-rate bonds are 0.07% per year for 2014 and 2013. 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, 2014, on the variable-rate bonds, plus expenses, for a total variable rate of .24%. The Corporation's allocable portion of the note premiums, net of discounts, is amortized over the term of the note using the straight-line method. Amortization on such amounts totaled $1,174,137 and $1,326,552 for the years ended December 31, 2014 and 2013, respectively.

On April 3, 2013, the Corporation closed a $125,000,000 mortgage loan with VALIC, 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 a new 1,000-room convention center hotel, and to fund the Convention District Projects including 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%. In March 2014, an additional $30,000,000 was drawn and bears interest at 4.78%. In July 2014 the final draw of $45,000,000 was funded and bears interest at 4.81%. The interest rates are effective through maturity.

9. 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.

10. 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"). The Management Agreement had a term of 15 years and commenced with the opening of the Hotel. Under the terms of the Management Agreement, the Hotel Operator agreed to manage, operate, and market the Hotel on behalf of the Corporation. For providing such services, the Hotel Operator received a management fee consisting of a base management fee and a subordinated management fee. The management fee adjusted annually based on the percent change in the competitive set's prior 12-month revenue per available room. During 2013, the base management fee expense increased $271,071 to $2,530,139.

The payment of the subordinated management fee under this agreement was 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 would be due and payable. The subordinated management fee expense totaled $1,351,751 for the year ended December 31, 2013. The cumulative accrued subordinated management fee of $9,441,742 is included in long-term liabilities at December 31, 2013.

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 year ended December 31, 2013, amortization of the deferred fee totaled $400,000 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, the deferred inducement fee from the Hotel Operator totaled $1,966,667.

On October 1, 2014, the Corporation executed a Management Agreement Termination Agreement (the "Termination Agreement") to terminate the Management Agreement as described above 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. The New Management Agreement is for 15 years and, consistent with the original Management Agreement, the New Management Agreement 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. The release of the unamortized inducement fee of $1,966,667 is recorded as other income as of December 31, 2014.

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 the Hotel Owner, for the development of an approximately 1,000-room new 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 no more than $62 million for the hotel site land and the loan commencing on January 5 following the year in which the hotel facility opens. See Note 6 above.

11. 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 to which it is exposed. 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.

The Corporation is a defendant in various pending lawsuits arising out of the conduct of its business. Management does not believe that the outcome of any of these matters will have a material adverse effect on the Corporation's financial position, results of operations, or cash flows.

12. SUBSEQUENT EVENTS

The Corporation has evaluated subsequent events for potential recognition and/or disclosures through September 10, 2015, the date the financial statements were available to be issued, and noted no matters other than the following:

On March 19, 2015, the City issued $132,590,000 of Convention & Entertainment Facilities Department Hotel Occupancy Tax (HOT) and Special Revenue Refunding Bonds, Series 2015. This issue included $99,620,000 Serial Bonds with stated interest rates between 2% - 5% maturing in various amounts from 2015 to 2035, and $32,970,000 of Term Bonds with stated interest rates between 4% - 5% maturing in various amounts from 2035 to 2044. The true interest cost was 3.3%. Proceeds were used to (a) refund a portion of the City's Outstanding Convention & Entertainment Facilities Department Hotel Occupancy Tax and Special Revenue Refunding Bonds, Series 2011, (b) refund outstanding commercial paper, (c) finance certain project costs, and (d) pay the costs of issuance of the Bonds. Net present value savings totaled $9.2 million or 13.1% of the refunded bonds.

* * * * * *