

Port of Houston Authority of Harris County, Texas
Notes to the Financial Statements
For the Years Ended December 31, 2002 and 2001
(in thousands)

1. Summary of Significant Accounting Policies

Reporting Entity

The Port of Houston Authority of Harris County, Texas (“Authority”) is an independent political subdivision created under the constitution of the state of Texas. The Port Commission, composed of seven commissioners, governs the Authority. Harris County, Texas (“County”) and the City of Houston, Texas (“City of Houston”) each appoint two commissioners to the Port Commission and jointly appoint the chairman. The City of Pasadena, Texas (“City of Pasadena”) and the Harris County Mayors and Councils Association (“Association”), representing 26 cities, each appoint one commissioner. Under state law, the County auditor serves as the auditor of the Authority and the County treasurer serves as the Treasurer of the Authority. The Authority is not a component unit of the County, the City of Houston, the City of Pasadena or the Association since none of these entities exercise financial accountability over the Authority. The Authority is considered a primary government entity since it satisfies all of the following criteria: (a) no entity appoints a voting majority of its governing body; (b) it is legally separate from other entities; and (c) it is fiscally independent of other state and local governments.

The financial statements of the Authority include all operations and activities of the Authority and its blended component units for which the Port Commission has financial accountability as defined above. Blended component units, although legally separate entities, are, in substance, part of the government’s operations.

Blended Component Units

The Port Development Corporation (“PDC”) was organized by the Authority under the State of Texas Development Corporation Act of 1979. PDC is a nonprofit corporation that issues industrial development revenue bonds to promote and develop commercial, industrial and manufacturing enterprises and to promote and encourage employment and public welfare. The issuance of any such bonds is approved by the Board of Directors (the “Board”) of PDC and the Texas Economic Development Commission (“TEDC”). Net earnings of PDC may be distributed to the Authority by action of the Board or upon dissolution of PDC. PDC is considered a blended component unit of the Authority as the governing boards of the Authority and PDC are substantially the same and the Authority is able to impose its will on PDC, as defined in Governmental Accounting Standards Board (“GASB”) Statement No. 14, The Financial Reporting Entity.

The Port of Houston Authority International Corporation (“POHAIC”), was organized during the fiscal year 2002 for the purpose of aiding, assisting and acting on behalf of the Authority in the performance of its governmental functions to promote the common good and general welfare of the Authority by providing consulting services to international port authorities and private businesses, including, but not limited to, terminal operators, engineering firms and construction companies, in the areas, among others, of trade development, administration,

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facilities, land, equipment, operations, security/protection and general management and to promote, develop, encourage and maintain employment, commerce and economic

development in the Authority. POHAIC is considered a blended component unit of the Authority under the provisions of GASB No. 14 as the Authority (1) appoints a voting majority of POHAIC's board, (2) is able to impose its will on POHAIC and (3) the board of the Authority and POHAIC are substantially the same.

Basis of Accounting

The Authority follows enterprise fund accounting and reporting requirements, including the accrual basis of accounting and application of all GASB pronouncements as well as the Financial Accounting Standards Board ("FASB") pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Operating revenues and expenses generally result from providing services in connection with ongoing operations. The principal revenues of the Authority are charges to customers for sales and services. The Authority also recognizes revenue in the form of rents and consulting fees. Operating expenses include the cost of services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

All cash and highly liquid time deposits and short-term investments with original maturities of three months or less when purchased are considered to be cash equivalents. Certificates of deposit with maturities over three months are considered time deposits.

Investments

All investments are recorded at fair value based upon quoted market prices with the difference between the purchase price and market price being recorded as interest income. For disclosure of custodial risk for all investments see Note 2 on Investments.

Trade Receivables

All trade receivables are shown net of an allowance for uncollectible accounts. Allowances are calculated using a two-part formula. An average of the last five years' bad debt write-

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offs is calculated. Since this number is usually small, approximately 100% of the accounts in excess of one year are added to derive an allowance that is reasonable.

Inventory

Inventory consists of materials and supplies and is stated at cost, determined on an average cost method.

Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

Deferred Dredging and Disposal Area Management Program (“DAMP”)

The cost of periodic maintenance dredging of berthing areas adjacent to the Authority’s wharves and of certain ship channels not maintained by the federal government is capitalized in deferred charges and amortized over three to four years.

DAMP costs represent the cost of preparing a disposal site for subsequent placing of dredged material on the site. Charges are accumulated during the preparation period and, when the site is completed, are capitalized in deferred charges and amortized over a five-year period.

Property Taxes

Property taxes (net of collection expenses) are used to pay debt service of the unlimited tax bonds. Property is appraised, and a lien on such property becomes enforceable, as of January 1, subject to certain procedures for rendition, appraisal, appraisal review and judicial review. Property taxes are levied September 1 for the year in which assessed. Taxes become delinquent February 1 of the following year and are subject to interest and penalty charges. The County bills and collects property taxes of the Authority for a fee and remits collections to the Authority. Property tax collection expenses incurred by the Authority for the years ended December 31, 2002 and 2001 were \$583 and \$769, respectively.

The tax rates for the years ended December 31, 2002 and 2001 were \$.01989 and \$.01826 per \$100 assessed valuation, respectively.

Restricted Assets

Restricted assets consist of capital and debt service restrictions. Restricted capital assets consist of the net proceeds in excess of unspent proceeds for unlimited tax improvement bonds. Restricted assets for debt service consist of proceeds available from taxes receivable as well as the proceeds from revenue bonds as stated in applicable bond covenants.

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Capital Assets

Capital assets are defined by the Authority as assets with an initial, individual cost of more than \$1 and an estimated useful life of one year or greater. Property constructed or acquired by purchase is stated at cost. Property received as a contribution is stated at estimated fair value on the date received.

The cost of normal maintenance and repairs that do not add value to the asset or materially extend asset lives are not capitalized. The Authority capitalizes, as a cost of its constructed assets, the interest expense of related borrowings less the interest earned on temporary investment of the proceeds of those borrowings from the date of borrowing. Capitalization increased the cost of assets constructed by the Authority by approximately \$5,440 and \$1,800 in 2002 and 2001, respectively.

Depreciation is computed using the straight-line method over the following useful lives:

Railroads	25-40 years
Buildings	20-40 years
Improvements other than Buildings	20-50 years
Machinery and equipment	3-20 years

Premiums (Discounts) on Bonds Payable and Issuance Costs

Effective January 1, 1997, issuance costs, premiums and discounts are amortized using the interest cost basis. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

Vacation and Sick Leave

Employees earn vacation at rates of 10 to 25 days per year and may accumulate a maximum of 20 to 50 days, depending on their length of employment. Upon termination, employees are paid for any unused accumulated vacation days at their current pay rate. Employees earn sick leave at the rate of 12 days per year. Upon termination or retirement, employees are paid for any unused sick leave days at their current pay rate up to a maximum of 60 days. With sufficient accruals, employees are allowed to receive payments at year-end of up to a maximum of 12 days of their unused sick leave, limited to \$.167 per day.

Reclassifications

Certain amounts for 2001 have been reclassified to conform with the 2002 presentation.

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New Pronouncements

In June 1999 the GASB issued Statement No. 34, “Basic Financial Statements Management Discussion and Analysis—for State and Local Governments.” The objective of this statement is to enhance the clarity and usefulness of the external financial reports of the state and local governments to the citizenry, legislative and oversight bodies, and investors and creditors. The Authority implemented GASB No. 34 for its fiscal year beginning January 1, 2002. Authority management believes that there has been no material adverse impact to the Authority’s financial position, results of operations or cash flows as a result of GASB No. 34, however, adoption of this statement significantly altered the presentation of certain financial information. As a result, net assets have been restated from the amounts previously reported to adopt the new accounting principle as follows:

	As Previously Reported	As Restated
At December 31, 2001 -		
Retained Earnings:		
Reserved for debt service		
Revenue bonds	\$3,225	
Unlimited tax bonds	27,341	
Reserved for revenue bond debt		
Retirement and contingency	5,826	
Unreserved retained earnings	504,278	
Contributed capital	20,321	
Invested in capital assets, net of related debt		\$337,229
Restricted net assets:		
Capital		26,872
Debt service		26,152
Unrestricted net assets		170,738
Total equity	\$560,991	
Total net assets		\$560,991

In April 2000 the GASB issued Statement No. 36, “Recipient Reporting for Certain Shared Non-exchange Revenues.” This is an amendment to GASB No. 33 in which recipient governments of derived tax revenues or imposed nonexchange revenues should recognize revenues for a period equal to cash received during the period and cash received after the end of a period should be recognized as revenues of the period. Adoption did not have a material impact on the Authority’s financial statements.

In June 2001 the GASB issued Statement No., 37, “Basic Financial Statements-and-Management’s Discussion and Analysis-for State and Local Governments: Omnibus.” This is an amendment of GASB No. 21 and GASB No. 34 and is to be implemented in

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conjunction with GASB No. 34 in fiscal year beginning January 1, 2002. Implementation of GASB No. 37 on January 1, 2002 did not have a material impact on the Authority's financial statements.

In June 2001 the GASB issued Statement No. 38, "Certain Financial Statement Note Disclosures." This Statement establishes and modifies disclosure requirements related to the summary of significant accounting policies, actions taken to address violation of significant finance-related legal and contractual provisions, debt and lease obligations, short-term debt, disaggregation of receivable and payable balances, and interfund balances and transfers. This statement was implemented in conjunction with GASB No. 34 in fiscal year beginning January 1, 2002.

In May 2002 the GASB issued Statement No. 39, "Determining Whether Certain Organizations Are Component Units—An Amendment of GASB Statement No. 14," which is effective for financial statements for periods beginning after June 15, 2003. GASB No. 39 amends GASB No. 14 to provide additional guidance to determine whether certain organizations for which the primary government is not financially accountable should be reported as component units based on the nature and significance of their relationship with the primary government. Management of the Authority does not believe that the adoption of GASB No. 39 will have a material impact on the financial statements of the Authority. This statement is effective for periods beginning after June 15, 2003.

GASB No. 40, "Deposit and Investment Risk Disclosures," was issued in March 2003 and addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, GASB No. 40 requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. The management of the Authority does not believe that the implementation of this statement will have a material effect on the financial statements of the Authority. This statement is effective for periods beginning after June 15, 2004.

2. Cash and Investments

The Authority's cash and cash equivalents balance of \$81,217 and \$76,589 as of December 31, 2002 and 2001, respectively, are maintained in demand accounts and mutual funds managed by a major fund manager. The bank balance at December 31, 2002 and 2001 was \$83,403 and \$78,994, respectively, of which the amount on deposit in demand accounts is fully covered by the federal deposit insurance through the FDIC or collateralized with securities held by the Authority's depository institution in joint safekeeping at the Federal Home Loan Bank of Dallas in the Authority's name. The mutual funds are invested primarily in direct obligations of the U.S. government or its agencies and are not subject to categorization in accordance with GASB No. 3, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools."

In accordance with authorized state statutes, the Authority invests in fully collateralized or insured time deposits, direct debt securities of the United States or its agencies, commercial paper, money market mutual funds, collateralized mortgage obligations, the underlying

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security for which is guaranteed by an agency of the United States, and fully collateralized repurchase agreements. The repurchase agreements must be purchased pursuant to a master repurchase agreement which specifies the rights and obligations of both parties and requires that the securities involved in the transactions be held in a safekeeping account subject to the control and custody of the Authority. Investments in security repurchase agreements may be made only with the Authority's depository bank or with state or national banks domiciled in the state of Texas. The Authority did not invest in repurchase agreements during 2002 or 2001.

The Authority's investments are categorized below to give an indication of the level of risk with Category 1 being the lowest level of risk to Category 3 being the highest level of risk. Investments are included in the credit risk categories as follows:

Category 1: Insured or registered or for which the securities are held by the Authority or its agent in the Authority's name.

Category 2: Uninsured and unregistered investments, with securities held by the Authority's counterparty's trust department or agent in the Authority's name.

Category 3: Uninsured and unregistered investments, with securities held by the Authority's counterparty, or by its trust department or agent, but not in the Authority's name.

Shown below are the Authority's investments by risk category as of December 31, 2002 and 2001:

	2002			
	Categories			
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Total</u>
U.S. Government				
Agencies Securities	\$274,434	\$0	\$0	\$274,434
Commerical Paper	2,509	0	0	2,509
Municipal Bonds	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u><u>\$276,943</u></u>	<u><u>\$0</u></u>	<u><u>\$0</u></u>	<u><u>276,943</u></u>

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	2001			Total
	1	Categories		
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Total</u>
U.S. Treasury Notes	\$43,277	\$0	\$0	\$43,277
U.S. Government				
Agencies Securities	210,622			210,622
Commerical Paper	18,269			18,269
Municipal Bonds	<u>11,901</u>			<u>11,901</u>
Total	<u><u>\$284,069</u></u>	<u><u>\$0</u></u>	<u><u>\$0</u></u>	<u><u>284,069</u></u>

3. Receivables

Receivables as of year end including the applicable allowances for uncollectible accounts are as follows:

Trade rceivables, net:	<u>2002</u>	<u>2001</u>
Trade accounts	\$17,141	\$21,718
Damage claims	1,177	913
Less allowance for doubtful accounts	<u>(1,307)</u>	<u>(1,389)</u>
Trade accounts, net	17,011	21,242
 Other receivables:		
Accrued receivables	7,168	0
Accrued interest	1,235	1,168
Other	<u>300</u>	<u>345</u>
Total other receivables	<u>8,703</u>	<u>1,513</u>
 Total receivables, net	<u><u>\$25,714</u></u>	<u><u>\$22,755</u></u>

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4. Sale of World Trade Building

In January 1999 the World Trade Center was sold by the Authority to Paladio Development Ltd, a Texas limited partnership, with Paladio Management Inc., a Texas corporation as the Sole General Partner, for the sum of \$4,000. The Authority received a down payment of \$400 and a promissory note for \$3,600 payable in nine equal installments of \$400 with the first installment due on or before one year from the date of the promissory note. The present value of this note as of December 31, 2002 totaled \$1,990 with approximately \$288 classified as current receivables and approximately \$1,702 in deferred charges. This transaction resulted in a deferred gain of approximately \$2,998, which totaled \$1,738 as of December 31, 2002. This balance will be written off in equal installments over the life of the promissory note.

5. Capital Assets

Capital asset activity for the year ended December 31, 2002 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$56,991	\$3,895	\$0	\$60,886
Channel improvements	92,026	14,619	0	106,645
Construction-in-progress	<u>128,541</u>	<u>55,879</u>	<u>58,217</u>	<u>126,203</u>
Total capital assets, not be depreciated	<u>277,558</u>	<u>74,393</u>	<u>58,217</u>	<u>293,734</u>
Capital assets, being depreciated:				
Buildings	64,699	747	0	65,446
Improvements other than buildings	328,058	8,234	150	336,142
Railroads	32,249	22,751	0	55,000
Machinery and equipment	<u>117,042</u>	<u>3,368</u>	<u>89</u>	<u>120,321</u>
Total capital assets, being depreciated	<u>542,048</u>	<u>35,100</u>	<u>239</u>	<u>576,909</u>
Less accumulated depreciation for:				
Buildings	(44,794)	(2,160)	0	(46,954)
Improvements other than buildings	(147,610)	(11,299)	42	(158,867)
Railroads	(18,990)	(1,279)	0	(20,269)
Machinery and equipment	<u>(66,525)</u>	<u>(5,866)</u>	<u>6</u>	<u>(72,385)</u>
Total accumulated depreciation	<u>(277,919)</u>	<u>(20,604)</u>	<u>48</u>	<u>(298,475)</u>
Total capital assets, being depreciated, net	<u>264,129</u>	<u>14,496</u>	<u>191</u>	<u>278,436</u>
Total capital assets, net	<u>\$541,687</u>	<u>\$88,889</u>	<u>\$58,408</u>	<u>\$572,168</u>

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Capital Asset activity for the year ended December 31, 2001 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$56,991	\$0	\$0	\$56,991
Channel improvements	55,721	36,305	0	92,026
Construction-in-progress	<u>167,862</u>	<u>22,450</u>	<u>61,771</u>	<u>128,541</u>
Total capital assets, not be depreciated	<u>280,574</u>	<u>58,755</u>	<u>61,771</u>	<u>277,558</u>
Capital assets, being depreciated:				
Buildings	62,581	2,121	3	64,699
Improvements other than buildings	288,247	40,424	613	328,059
Railroads	31,189	1,060	0	32,249
Machinery and equipment	<u>108,594</u>	<u>8,684</u>	<u>236</u>	<u>117,042</u>
Total capital assets, being depreciated	<u>490,611</u>	<u>52,289</u>	<u>852</u>	<u>542,048</u>
Less accumulated depreciation for:				
Buildings	(42,683)	(2,111)	0	(44,794)
Improvements other than buildings	(136,146)	(11,464)	0	(147,610)
Railroads	(18,233)	(757)	0	(18,990)
Machinery and equipment	<u>(60,523)</u>	<u>(6,238)</u>	<u>236</u>	<u>(66,525)</u>
Total accumulated depreciation	<u>(257,585)</u>	<u>(20,570)</u>	<u>236</u>	<u>(277,919)</u>
Total capital assets, being depreciated, net	<u>233,027</u>	<u>31,719</u>	<u>616</u>	<u>264,129</u>
Total capital assets, net	<u><u>\$513,600</u></u>	<u><u>\$90,474</u></u>	<u><u>\$62,387</u></u>	<u><u>\$541,687</u></u>

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6. Operating Leases

The Authority leases to others some of its land, buildings and improvements and cargo handling equipment. As of December 31, 2002, minimum rental payments to be received by the Authority under the operating leases that have initial or remaining noncancelable lease terms in excess of one year are as follows :

2003	\$ 11,098
2004	9,109
2005	8,229
2006	7,393
2007	6,511
Thereafter	<u>73,188</u>
Total	<u>\$115,528</u>

In addition, the Port Terminal Railroad Association (“PTRA”) leases certain railroad facilities from the Authority under a ten-year renewable agreement. The agreement provides for a yearly adjustment in rent on August 1, based on the percentage change in the Producer Price Index (all commodities) from the previous August 1. Effective August 1, 2002, the monthly rental is \$110. The Authority invoiced PTRA approximately \$1,322 and \$1,325 under this agreement in 2002 and 2001, respectively.

7. Capital Lease Commitments

On July 21, 1997, the Authority entered into a 20-year lease agreement with the Board of Trustees of the Galveston Wharves for its East End Container Terminal located at Pier 10. Contained in the agreement is a provision that various fixed assets, including several container and yard cranes, tractors, trailers, and other equipment, which will become property of the Authority after 15 years. The Authority also began leasing computer equipment in July 1997 that results in the transfer of ownership to the Authority at the conclusion of the lease. Both are classified as capital leases. The total present value of lease payments as of December 31, 2002 was approximately \$3,802 and consisted of approximately \$477 in current liabilities and approximately \$3,325 in noncurrent liabilities. Future minimum lease payments are as follows for the years ended December 31:

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2003	\$674
2004	648
2005	599
2006	543
2007	488
2008 - 2012	<u>1,785</u>
Total Lease Payments	4,737
Less: Amount representing interest	<u>(935)</u>
 Present value of minimum lease payments	 <u><u>\$3,802</u></u>

Cost of assets under lease are \$6,430 with accumulated depreciation of \$2,770 and current year depreciation of \$491.

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8. Long-Term Debt and Noncurrent Liabilities

Changes in Long-Term Liabilities - 2002

	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Bonds Payable					
Revenue Bonds	\$22,365	\$17,175	\$22,205	\$17,335	\$4,320
General Obligation Bonds	324,705	23,060	16,110	331,655	25,410
Less deferred amounts:	<u>1,587</u>	<u>636</u>	<u>274</u>	<u>1,949</u>	
Total Bonds Payable	<u>348,657</u>	<u>40,871</u>	<u>38,589</u>	<u>350,939</u>	<u>29,730</u>
Other noncurrent liabilities:					
Capital Leases	4,317		515	3,802	477 (1)
Compensated Absences	3,865	738	618	3,985	244 (1)
Advances from Developer	16,328		1,138	15,190	0
Other	<u>328</u>		<u>8</u>	<u>320</u>	<u>0</u>
Total other noncurrent liabilities	<u>\$24,838</u>	<u>\$738</u>	<u>\$2,279</u>	<u>\$23,297</u>	<u>\$721</u>

Changes in Long-Term Liabilities - 2001

	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Bonds Payable					
Revenue Bonds	\$26,590		\$4,225	\$22,365	\$4,710
General Obligation Bonds	263,475	87,300	26,070	324,705	16,110
Less deferred amounts:	<u>1,017</u>	<u>680</u>	<u>110</u>	<u>1,587</u>	
Total Bonds Payable	<u>291,082</u>	<u>87,980</u>	<u>30,405</u>	<u>348,657</u>	<u>20,820</u>
Other noncurrent liabilities:					
Capital Leases	4,860		543	4,317	515 (1)
Compensated Absences	3,339	1,202	676	3,865	221 (1)
Advances from Developer	13,896	3,643	1,211	16,328	0
Other	<u>110</u>	<u>218</u>		<u>328</u>	<u>0</u>
Total other noncurrent liabilities	<u>\$22,205</u>	<u>\$5,063</u>	<u>\$2,430</u>	<u>\$24,838</u>	<u>\$736</u>

(1) Included in accounts payable and other noncurrent liabilities

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Long - Term Debt

Outstanding Long - Term Debt

Long - Term Debt is summarized as follows (in thousands):

	<u>Original Issue</u>	<u>Interest Rate %</u>	<u>Issue Date</u>	<u>Maturity</u>	<u>December 31</u>	
					<u>2002</u>	<u>2001</u>
Revenue Bonds:						
Series 1997	25,000	3.50 - 7.00	02/01/77	2002	\$0	\$2,600
Series 1992, Refunding	32,280	3.80 - 6.50	02/26/92	2006	0	19,525
Series 2002, Refunding	22,285	2.00 - 5.00	02/20/02	2013	17,175	0
Special Purpose Revenue Bonds-						
Series 1964	1,900	2.50	07/01/64	2004	160	240
Total Revenue Bonds					17,335	22,365
Less Unamortized Discounts					542	(94)
Revenue Bonds, Net					17,877	22,271
Unlimited Tax Refunding Bonds:						
Series 1997 *	28,000	4.75 - 5.00	10/23/97	2013	22,315	25,525
Series 1999B	6,435	5.00 - 5.25	09/28/99	2009	4,365	5,045
Series 2000B	8,700	4.55 - 5.50	10/15/00	2011	6,755	7,565
Series 2002B	7,060	5.50 - 4.25	12/12/02	2013	7,060	0
Total Unlimited Tax Refunding Bonds					40,495	38,135
Add (Subtract) Unamortized Premiums/(Discounts) and Deferred Loss					943	945
Unlimited Tax Refunding Bonds, Net					41,438	39,080
Unlimited Tax Port Improvement Bonds:						
Series 1992A	1,000	5.50 - 7.50	01/07/92	2013	5,785	6,315
Series 1992B	1,000	5.60 - 7.60	12/01/92	2013	1,275	1,800
Series 1994	15,000	6.50 - 8.50	12/01/94	2016	10,500	11,250
Series 1995	12,000	4.90 - 6.90	11/01/95	2017	9,000	9,600
Series 1996	42,000	5.50 - 7.50	04/01/96	2017	39,000	41,600
Series 1997	28,000	4.80 - 5.375	07/09/97	2018	22,400	23,800
Series 1998A	81,000	3.80 - 5.00	11/17/98	2019	68,850	72,900
Series 1998B	7,000	3.40 - 5.40	11/17/98	2019	5,950	6,300
Series 1999A	14,000	5.5	09/28/99	2024	13,395	13,705
Series 2000A	12,000	4.25 - 5.10	10/15/00	2024	11,705	12,000
Series 2001A	17,000	5.0	11/01/01	2026	17,300	17,300
Series 2001B	70,000	4.00 - 5.00	11/01/01	2026	70,000	70,000
Series 2002 A	16,000	3.00 - 5.00	12/12/02	2027	16,000	0
					291,160	286,570
Add Unamortized Premiums/(Discounts)					464	736
					291,624	287,306
Total Long-Term Debt					350,939	348,657
Less Current Maturities					(29,730)	(20,820)
Long - Term Debt (net of unamortized premium/(discount)					\$321,209	\$327,837

* The Refunding Bonds, Series 1997A, consist of \$19,830,000 Current Interest Bonds at 4.75 - 5.00 to mature 2000 - 2013 and \$ 2,485,000 Capital Appreciation Bond at 4.80 - 4.85 to mature 2006 - 2007.

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All of the net revenues of the Authority are pledged for the payment of debt service of the revenue bonds (“first-lien bonds”). Net revenues, as defined by the various bond resolutions include substantially all of the Authority’s revenues and expenses other than those related to (a) the Bayport operations, (b) interest earned on certain bond funds, (c) revenues from property taxes levied by the Authority, (d) interest expense on revenue and unlimited tax bonds, and (e) depreciation and amortization. The revenue bond resolutions further require that the net revenues, as defined, equal at least 150% of the average annual debt service on the first-lien bonds before additional first-lien bonds can be sold. Net revenues for 2002 and 2001 were 494% and 900% of the respective year’s average annual debt service.

All of the net revenues, as defined, from the Bayport operations (see Note 9) are pledged for the payment of debt service of the Special Purpose Revenue Bonds, Series 1964.

There is no legal debt margin as to the issuance of the unlimited tax bonds.

Debt Service Requirements

Total debt service requirements as of December 31, 2002 are as follows:

Year Ending	Bond Principal		Bond Interest		Total
	Revenue	Unlimited Tax	Revenue	Unlimited Tax	
December 31					
2003	\$4,320	\$25,410	\$702	\$16,406	\$46,838
2004	4,395	18,345	515	15,564	38,819
2005	4,265	18,820	307	14,629	38,021
2006	4,355	16,665	101	15,924	37,045
2007	-	16,450	-	15,269	31,719
2008-2012	-	85,660	-	51,674	137,334
2013-2017	-	75,230	-	31,256	106,486
2018-2022	-	43,925	-	14,171	58,096
2023-2027	-	31,150	-	4,017	35,167
Total	\$17,335	\$331,655	\$1,625	\$178,910	\$529,525

All bonds generally mature serially based on stated maturity dates. However, all bonds may be redeemed prior to their maturities in accordance with provisions of the various bond resolutions at par.

At December 31, 2002, the Authority had \$25,700 remaining of the \$130,000 in authorized but not issued unlimited tax bonds for improvement to the Houston Ship Channel, which were approved by voters in an election in November 1989.

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At December 31, 2002, the Authority also had \$317,000 remaining of the \$387,000 in authorized but not issued unlimited tax bonds for construction which was approved by the voters in an election in November 1999.

Outstanding Industrial Development Revenue Bonds

PDC has issued bonds on behalf of various users to promote industrial development. Each bond issue includes a covenant that indemnifies PDC and the Authority against any and all losses related to the projects funded by the bond. The bonds are payable solely by payments from the users, as defined under the loan agreements, and PDC is under no obligation to repay the bonds from any other source. All payments are made directly by the users to the trustees. The balance of such bonds outstanding was \$47,370,000 as of December 31, 2002 and 2001, according to information received from the trustees. No bond was written off as uncollectible during 2002.

Revenue Bonds Outstanding

Receiving Entity	Date Issued	Interest Rate	Maturity Date	Amount Issued	Balance
Ashland Oil, Inc.	10/01/83	Variable	10/01/03	\$4,700	\$4,700
Mine Safety Applincance Co.	12/01/83	Variable	01/01/09	750	750
Mitsui & co. U.S.A., Inc	12/03/85	Variable	12/01/05	15,100	15,100
Mitsui & co. U.S.A., Inc	12/06/85	Variable	12/01/05	4,400	4,400
Pasadena Terminal Company, Inc.	12/01/84	Variable	12/01/04	40,000	12,820
Stolt Terminals (Houston)	01/11/89	Variable	01/15/14	9,600	9,600
Total				<u>\$74,550</u>	<u>\$47,370</u>

Bond Refundings

At various times the Authority defeased certain bonds by placing the proceeds of new bonds, together with other available funds, in an irrevocable escrow with a trustee to provide for all future debt service on the refunded bonds. Accordingly, the trust account assets and the liabilities for the bonds to be defeased are not included in the Authority's financial statements. At December 31, 2002, the outstanding balance of the defeased unlimited tax bond was \$39,500.

During 2002, the Authority issued \$7,060 of unlimited tax refunding bonds and used the proceeds, net of issuance cost, to establish an irrevocable escrow fund to provide for all future debt service requirements on the outstanding tax bond, Series 1992, that will be refunded in

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January 2003. As a result, the Series 1992 bonds will be considered to be defeased and the liability for such bonds will be removed from the financial statements of the Authority in 2003. At December 31, 2002, the outstanding balance of these tax refunding bonds to be defeased is \$7,060. The gain of \$15 will be realized on the refunding in January 2003 and will be amortized on an interest cost basis over the life of the bond issue which runs through October 1, 2013. The gain was determined as follows :

Principal balance of refunded bonds		\$7,060
Less:		
Total payments to trustee:		
Face amount of refunding issue	\$7,060	
Premium received	150	
Issuance Costs	<u>(57)</u>	
Total	7,153	
Accrued interest payable	<u>(108)</u>	<u>(7,045)</u>
Deferred gain on refunding		<u>\$ 15</u>

The Authority reduced its aggregate debt service payments by approximately \$782 over the next ten years and obtained an economic gain (the difference between the present values of the old and new debt service payments) of approximately \$650.

Also during 2002, the Authority issued \$22,285 of revenue refunding bonds and used the proceeds, net of issuance costs, to establish an irrevocable escrow fund to provide for all future debt service requirements on the outstanding revenue refunding bonds, Series 1992 and revenue bonds Series 1977 that were refunded in May, 2002. As a result, the series refunding bonds, Series 1992 and the revenue bond Series 1977 were considered to be defeased and the liability for such bonds were removed from the financial statements of the Authority in 2002. The outstanding balance of the defeased bonds were \$22,125. A gain of \$72 was realized on the refunding and will be amortized on an interest cost basis over the life of the bond issue which runs through May 1, 2006. The gain was determined as follows:

Principal balance of refunded bonds		\$22,125
Less:		
Total payments to trustee:		
Face amount of refunding issue	\$22,285	
Premium received	840	
Issuance Costs	<u>(374)</u>	
Total	22,751	
Accrued interest payable	<u>(698)</u>	<u>(22,053)</u>
Deferred gain on refunding		<u>\$ 72</u>
Bond Restrictions		

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The bond resolutions require that during the period in which the bonds are outstanding, the Authority must create and maintain certain accounts (“funds”) to receive the proceeds from the sale of the bonds, property taxes levied and the net revenues, as defined, derived from the operation of the Authority’s facilities. These assets can be used only in accordance with the terms of the bond resolutions to pay the capital costs of enlarging, extending or improving the Authority’s facilities or to pay the debt service cost of the related bonds.

Arbitrage

The Federal Tax Reform Act of 1986 requires issuers of tax-exempt debt to make payments to the U.S. Treasury of investment income received at yields that exceed the issuer’s tax-exempt borrowing rates. The U.S. Treasury requires payment for each issue every five years. Arbitrage liability for tax-exempt debt subject to the Tax Reform Act issued through December 31, 2002 amounted to \$3. The estimated liability is updated annually for any tax-exempt issuance or changes in yields until payment of the calculated liability is due.

9. Bayport Facilities

Certain land and port facilities of the Bayport division were acquired or constructed using the proceeds from the Special Purpose Revenue bonds, Series 1964, and interest-free advances (including the interest earnings on the invested portions thereof) from the developer of an adjacent industrial park. The developer also agreed to advance to the Authority amounts necessary to cover maintenance and operating expenses of the Bayport facilities if, and to the extent that, gross revenues from the operations of the Bayport facilities were insufficient. Such construction and operating advances amounted to approximately \$15,190 at December 31, 2002 and \$16,328 at December 31, 2001. All such advances will be repaid only from net revenues, if any, of the Bayport division earned through the year 2013.

Effective October 27, 1997, the Authority, the developer, and the Bayport operators entered into an Agreement of Compromise and Settlement (the “Agreement”) that resolves various legal disputes in connection with the Authority’s property at Bayport, including disputes as to reimbursement of the developer for amounts previously advanced. The Agreement provides for an increased user fee (from 22¢ per ton of liquid to 24¢) to be credited to the Bayport reimbursement account through July 31, 2013. All proceeds of this fee will be used for payment of amounts then due upon the Special Purpose Revenue Bonds, Series 1964, for payment of certain of the Authority’s operating expenses relating to Bayport, and for the repayment of amounts advanced to the Authority by the developer. The Agreement limits repayments to the developer to the sum of \$21,500 (plus any additional advances made by the developer) and also provides that all repayment obligations of the Authority to the developer shall finally terminate on July 13, 2013. The Agreement provided for the payment of \$2,232 by the Authority to the developer in exchange for the developer’s final release of all of the developer’s rights concerning the Authority’s property at Bayport. The Agreement contains various other provisions, including provisions addressing allocation of maintenance costs for

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the Bayport Channel and Turning Basin among the Authority, the developer and Private Operators at Bayport. The Agreement supersedes all prior agreements between the Authority and developer and was contingent upon the U.S. Corps of Engineers' approval of offshore disposal of Bayport dredge material. Such approval was received in October of 1998.

The Authority had recorded approximately \$19,900 in advances from the developer at the time the new agreement was signed and has not recorded the additional \$1,600 in possible repayments since management does not, at this time, believe that such future net revenues will be sufficient to pay all of the currently existing advances. The repayments during the 12 months ending December 31, 2002 and 2001 were approximately \$1,138 and \$1,211, respectively.

10. Retirement Plan

Plan Description

The Port of Houston Authority Restated Retirement Plan ("Plan") is a single-employer noncontributory defined benefit retirement plan covering all permanent, full-time employees after the completion of one year of employment. The Authority's Port Commission, the Pension Committee and Melanie Sherman, the plan administrator, control and manage the operation and administration of the Plan. Compass Bank (the Trustee") serves as the trustee of the Plan. The Plan issues a stand-alone financial report that may be obtained by requesting such report from the Port of Houston Authority of Harris County, P.O. Box 2562, Houston, TX 77252, Attention: Controller. Employees vest in the Plan after five years of continuous service with the Authority. The Authority's payroll for employees covered by the Plan for the plan years ended July 31, 2002 and 2001 was \$20,257 (80% of the total payroll of \$25,285) and \$18,779 (82% of total payroll of \$22,825), respectively.

Vested employees who retire at age 65 are entitled to an annual retirement benefit, payable monthly, for five years certain and for life thereafter, in an amount equal to the lesser of 2.3% of their average monthly base earnings, multiplied by their number of years of credited service, or 70% of the average monthly base earnings. Monthly base earnings are those of the highest consecutive five years out of the ten years immediately preceding retirement. The Plan also provides early and late retirement options with benefits adjusted accordingly, as well as death and disability benefits. These benefit provisions and all other plan requirements are established and approved by the Port Commission.

Actuarially Determined Contribution Requirements and Contributions Made

The Authority's funding policy provides for actuarially determined annual contributions, which include the normal cost and amortization of the unfounded frozen actuarial accrued liability.

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Actuarial Valuation Method

Actuarial Valuation Date	08/01/02	08/01/01	08/01/00
Actuarial Cost Method	Entry Age	Entry Age	Entry Age
Amortization Method	Level Dollar, (closed)	Level Dollar, (closed)	Level Dollar, (closed)
Amortization Period in Years	30	30	30
Asset Valuation Method	Market Value	Market Value	Market Value
Actuarial Assumptions:			
Investment Return	7.5%	7.5%	7.5%
Projected Salary Increases	3.0% - 8.0%	3.0% - 8.0%	3.0% - 8.0%
Inflation	3.5%	3.5%	3.5%
Cost of Living Adjustment	None	None	None

The required contributions to the Plan, including payments of the unfunded actuarial accrued liability, are actuarially determined as if the Authority were subject to Sections 412 and 404 of the Internal Revenue Code, even though the Authority is not subject to these rules.

Components of the unfunded actuarial liability are amortized as level dollar amounts using the closed basis. Components consisting of actuarial gains and losses are amortized over five years. Components consisting of amendments are amortized over 30 years, except the 8/95 amendment that is amortized over 5 years. Components consisting of revised assumptions are amortized over ten years. Components consisting of revised actuarial methods are amortized over 30 years. The resulting equivalent single amortization base is amortized over a maximum of 30 years.

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Plan Statistics
For Plan Years July 31, 2002, 2001, and 2000
Actuarial Valuation Report As of August 1, 2002, 2001, and 2000

	<u>2002</u>	<u>% Covered Payroll</u>	<u>2001</u>	<u>% Covered Payroll</u>	<u>2000</u>	<u>% Covered Payroll</u>
Actuarial Determined Employer Contribution Normal Cost	\$1,334	6.6%	\$1,259	6.7%	\$1,169	6.4%
Annual Pension Cost	\$3,229		\$2,136		\$1,127	
% of APC Contributed	100%		100%		100%	
NPO	None		None		None	

11. Postretirement Benefits

In addition to providing pension benefits, the Authority provides certain postretirement health care and life insurance benefits for the retired employees and their spouses through provisions enacted by the authority of the Port Commission. At December 31, 2002, 240 former employees were eligible for these benefits. The Authority funds all of the premiums for retiree life insurance and a portion of the health insurance premiums. Continuation of these benefits and the Authority's contributions are dependent on periodic authorization by the Port Commission.

The health insurance benefits provided to retirees are the same as those offered to active employees though retirees have the option of securing their own insurance and receiving a monthly reimbursement from the Authority for a portion of the costs. The supplied benefits include hospital, doctor and prescription drug charges.

Basic life insurance coverage provided to retirees is based upon the retirees' annual compensation at retirement. Active employees receive life insurance coverage valued at 150% of their current annual salary. Retirees receive life insurance coverage valued at \$5,000, \$10,000 or \$15,000 based on the salary at retirement date.

For the fiscal years ended December 31, 2002 and 2001, the cost of retiree health benefits, recorded on a pay-as-you-go basis and net of contributions from retirees, was \$1,538 and \$1,293, respectively. Retiree life benefit costs were \$12 for 2002 and 2001.

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12. Risk Management

The Authority is exposed to risk of financial loss from fire, windstorm, explosion and other perils that could damage or destroy assets and properties and cause loss of income should assets and properties be shut down for an extended period of time. The Authority is also exposed to third-party bodily injury and property damage claims arising from the operation and ownership of its properties and from losses resulting from on-the-job injuries sustained by employees.

The Authority has purchased retrospective-rated insurance policies for workers compensation, general liability and automobile liability. At December 31, 2002, the Authority was insured for the following loss limitations:

	Workers' Compensation	General Liability	Automobile Liability
Per Accident	\$200	\$100	\$100
Bodily Injury	Not Applicable	200	200

The Authority's insurance policy also includes a maximum loss liability provision of \$2,690 for the period from March 1, 2002 through February 28, 2003. Settled claims did not exceed the insurance coverage during the last three fiscal years.

The claims liability of \$37 reported at December 31, 2002, is based on the requirements of GASB No. 10, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Such liability was actuarially determined. The liability includes amounts for claims that have been incurred but not reported.

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Changes in claim liability amounts in fiscal years 2002 and 2001 were as follows:

	2002	2001
Unpaid claims and claim adjustment		
Expenses at beginning of year	\$714	\$444
Incurred claims and claim adjustment expenses:		
Provision for insured events of the current year	557	565
Changes in provision for insured events of prior years	(327)	483
Total incurred claims and claim adjustment expenses	230	1,048
Payments:		
Claims and claim adjustment expenses attributable to insured events of the current year	566	381
Claims and claim adjustment refunds attributable to insured events of prior ears	341	397
Total payment	907	778
Total unpaid claims and claim adjustment Expenses at year end	\$37	\$714

13. Commitments and Contingencies

Commitments

At December 31 2002 the Authority had committed approximately \$66,000 for supplies, services, the purchase of equipment and the expansion of facilities.

Litigation and Claims

The Authority is the defendant in various legal actions that arise in the normal course of business. No prediction as to the result of such litigation or claims can be made, but the Authority, based on consultation with outside counsel, believes the outcome of such matters will not materially affect its financial position.

There is a possible unasserted claim for remediation of contamination on the Port's property that could be brought by federal and/or state agencies. The Authority has sustained groundwater and soil contamination of its property due to the releases of hazardous chemicals from a pesticide facility adjacent to the Authority's property. The Authority has not manufactured, generated, or released such hazardous substances, nor has it contracted with the plant facility to use or manufacture any of the substances that have caused the contamination. Therefore, the Authority has taken the position that it is an innocent land owner as that term is defined by the laws of the state of Texas and that it is exempt from liability for site cleanup. Management of the Authority

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believes it is unlikely that any federal or state agency will assert the Authority liability for the clean up of contaminants from the adjacent pesticide facility which has migrated on to the Port property.

The Authority is the plaintiff in a case against GB BioSciences, et al., alleging that for almost 50 years the GB Biosciences' facility has manufactured pesticides and disposed of chemical wastes in areas owned, operated or controlled by them. The GB BioSciences' facility and its disposal areas are directly adjacent to a number of separate tracts of land owned by the Authority. The GB BioSciences' facility has contaminated these properties. The Authority's lawsuit seeks recovery of the Authority's investigative and legal fees and other costs associated with this matter, damages (including property and punitive damages), declaratory judgment, and to have GB BioSciences, et al ordered to abate, remove and remediate all contamination. Trial is set for January 2004.

The Authority was served as a defendant in United States District Court for the Southern District of Texas. The plaintiffs are pipeline companies that own pipelines crossing the Houston Ship Channel at various points. The pipeline companies allege the cost of removal or relocation of their pipelines in order to widen and deepen the Houston Ship Channel should be borne by the Authority. The federal district court entered final judgment against the Authority concluding that the Authority and not the pipeline companies, is responsible for the cost of pipeline removal or relocation. The federal district court's judgment was nonmonetary. The Authority and the U.S. Army Corps of Engineers are appealing the district court judgment to the United States Court of Appeals for the Fifth Circuit. The Authority cannot predict the final outcome of the appeal.

Required Supplementary Information

**Port of Houston Authority Restated Retirement Plan
Schedule of Funding Progress**

a) Actuarial Valuation Date	08/01/02	08/01/01	08/01/00
b) Actuarial Value of Assets	\$59,638	\$64,678	\$70,309
c) Actuarial Accrued Liability (AAL)	\$80,188	\$77,034	\$73,453
d) Unfunded (Overfunded) Actuarial Accrued Liability (UAAL) (c – b)	\$20,550	\$12,356	\$ 3,143
e) Funded Ratio (b / c)	74.4%	84.0%	95.7%
f) Annual Covered Payroll (Actuarial)	\$20,257	\$18,779	\$17,550
g) UAAL as a % of Covered Payroll (d / f)	101.4%	65.8%	17.9.0%

