**NEW ISSUES- BOOK- ENTRY ONLY** **RATINGS: See "RATINGS" herein**

**OFFICIAL STATEMENT DATED AUGUST 24, 2005**

*In the opinion of Bond Counsel, (i) interest on the Series 2005A Bonds and Series 2005B Bonds is excludable from gross income for federal income tax purposes under existing law, subject to the matters described under "Tax Matters" herein, (ii) interest on the Series 2005A Bonds is an item of tax preference for purposes of determining the alternative minimum tax imposed on individuals and corporations, and (iii) interest on the Series 2005B Bonds is not includable in the alternative minimum taxable income of individuals. See "TAX MATTERS" for a discussion of the opinions of Bond Counsel, including the alternative minimum tax on individuals and corporations.*

# PORT OF HOUSTON AUTHORITY
# OF
# HARRIS COUNTY, TEXAS

**(A political subdivision of the State of Texas having boundaries coterminous with Harris County)**

| **\$36,665,000<br>UNLIMITED TAX REFUNDING BONDS,<br>SERIES 2005A (AMT)** | **\$62,485,000<br>UNLIMITED TAX REFUNDING BONDS,<br>SERIES 2005B (NON-AMT)** |
|---|---|

**Interest Accrual Date: Date of Delivery** **Due: October 1, as shown on the inside cover page**

The \$36,665,000 "Port of Houston Authority of Harris County, Texas Unlimited Tax Refunding Bonds, Series 2005A (AMT)" (the "Series 2005A Bonds") and \$62,485,000 "Port of Houston Authority of Harris County, Texas, Unlimited Tax Refunding Bonds, Series 2005B (NON-AMT)" (the "Series 2005B Bonds") (collectively, the "Bonds") are hereby offered for sale by the Port of Houston Authority of Harris County, Texas (the "Authority"). The Bonds are payable from the receipts of separate annual ad valorem taxes, without legal limit as to rate, levied on taxable property within the Authority. The Bonds are not issued by, nor are they in any way obligations of, Harris County, Texas. See "DESCRIPTION OF THE BONDS— Source of Payment of the Bonds" herein.

The Bonds will be issued only in fully-registered form in the denomination of \$5,000, or integral multiples thereof, initially registered solely in the name of Cede & Co., as registered owner and nominee for The Depository Trust Company ("DTC"), New York, New York, acting as securities depository for the Bonds, until DTC resigns or is discharged. The Bonds initially will be available to purchasers in book-entry form only. So long as Cede & Co., as nominee for DTC, is the registered owner of the Bonds, the Bonds will be payable to Cede & Co., which will, in turn, remit such amounts to DTC participants for subsequent disbursement to the beneficial owners of the Bonds. See "DESCRIPTION OF THE BONDS—Book-Entry-Only System" herein.

Interest on the Bonds accrues from the date of delivery and is payable on April 1, 2006, and on each April 1 and October 1 thereafter until the earlier of maturity or redemption, by check mailed to the registered owner of record as of the 15th day of the month next preceding each interest payment date. JPMorgan Chase Bank, National Association, Dallas, Texas, is the initial paying agent/registrar (the "Paying Agent/Registrar") for the Bonds. Principal of the Bonds is payable upon presentation of the Bonds to the Paying Agent/Registrar at maturity or earlier redemption date. See "DESCRIPTION OF BONDS—General."

Proceeds of the Bonds will be used to refund all or a portion of the commercial paper notes of the Authority (the "Refunded Notes") and certain outstanding bonds of the Authority more particularly described in "APPENDIX E—Schedule of Refunded Bonds" (the "Refunded Bonds") and to pay costs of issuance. See "PLAN OF FINANCING."

The Bonds are subject to redemption prior to maturity as described herein. See "DESCRIPTION OF THE BONDS— Redemption."

**MBIA** The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by MBIA Insurance Corporation (see "BOND INSURANCE" herein).

**SEE INSIDE COVER PAGE FOR MATURITY AND PRICING SCHEDULES AND CUSIP NUMBERS**

The Bonds are offered for delivery, when, as and if issued by the Authority, subject to the approving opinions of the Attorney General of Texas, and the opinions of Andrews Kurth LLP, Houston, Texas, Bond Counsel. Certain legal matters will be passed upon for the Underwriters by Winstead Sechrest & Minick P.C., Houston, Texas. The Bonds are expected to be available for delivery through DTC on or about September 8, 2005.

**LEHMAN BROTHERS** **SIEBERT BRANDFORD SHANK & CO., LLC**

**FIRST ALBANY CAPITAL INC.** **MERRILL LYNCH & CO.**
**MORGAN KEEGAN & COMPANY, INC.** **RBC DAIN RAUSCHER**

## MATURITY SCHEDULE, PRINCIPAL AMOUNTS, INTEREST RATES, YIELDS, AND CUSIP NUMBERS

### $36,665,000 UNLIMITED TAX REFUNDING BONDS, SERIES 2005A (AMT)

| Maturity Date October 1 | Principal Amount | Interest Rate | Initial Offering Price/Yield | CUSIP Number[b] |
|---|---|---|---|---|
| 2014 | $ 3,920,000 | 5.000% | 3.950% | 734260 G22 |
| 2015 | 4,515,000 | 5.000 | 4.030 | 734260 G 30 |
| 2016 | 5,145,000 | 5.000 | 4.100[a] | 734260 G 48 |
| 2017 | 6,480,000 | 4.000 | 4.250 | 734260 G 55 |
| 2018 | 9,695,000 | 5.000 | 4.170[a] | 734260 G 63 |
| 2019 | 5,160,000 | 5.000 | 4.190[a] | 734260 G 71 |
| *** | *** | *** | *** | *** |
| 2023 | 1,750,000 | 4.250 | 4.500 | 734260 G 89 |

### $62,485,000 UNLIMITED TAX REFUNDING BONDS, SERIES 2005B (NON-AMT)

| Maturity Date October 1 | Principal Amount | Interest Rate | Initial Offering Price/Yield | CUSIP Number[b] |
|---|---|---|---|---|
| 2012 | $ 1,815,000 | 5.000% | 3.570% | 734260 G 97 |
| 2013 | 2,355,000 | 5.000 | 3.660 | 734260 H 21 |
| *** | *** | *** | *** | *** |
| 2019 | 5,230,000 | 5.000 | 4.040[a] | 734260 H 39 |
| 2020 | 15,165,000 | 5.000 | 4.060[a] | 734260 H 47 |
| 2021 | 15,915,000 | 5.000 | 4.090[a] | 734260 H 54 |
| 2022[c] | 6,005,000 | 5.000 | 4.120[a] | 734260 H 62 |
| 2022[c] | 10,000,000 | 4.750 | 4.230[a] | 734260 H 70 |
| 2023 | 6,000,000 | 4.125 | 4.410 | 734260 H 88 |

The Bonds maturing on or after October 1, 2016 are subject to redemption at the option of the Authority on October 1, 2015 or on any date thereafter at the the par value thereof plus accrued interest to the date fixed for redemption, upon 30 days written notice to the registered owners thereof. See "DESCRIPTION OF THE BONDS — Redemption."

(a) The initial offering prices or yields of the Bonds are calculated to the first optional redemption date.

(b) Copyright 2005, American Bankers Association. CUSIP numbers have been assigned to the Bonds by Standard and Poor's CUSIP Service Bureau, a division of the McGraw-Hill Companies, Inc. and are included solely for the convenience of the owners of the Bonds. Neither the Authority, the Financial Advisor, nor the Underwriters are responsible for the selection or correctness of the CUSIP numbers set forth herein.

(c) Split maturity.

No dealer, broker, salesperson or other person has been authorized to give information or to make any representation with respect to the Bonds to be issued, other than those contained in this Official Statement, and, if given or made, such other information or representations not so authorized must not be relied upon as having been given or authorized by the Authority or the Underwriters.

This Official Statement is not to be used in connection with an offer to sell or the solicitation of an offer to buy, nor will there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

All financial and other information presented herein, except for the information expressly attributed to other sources, has been provided by the Authority from its records and is intended to show recent historical information. Such information is not guaranteed as to accuracy or completeness. No representation is made that past performance, as might be shown by such financial and other information, will necessarily continue or be expected in the future. All descriptions of laws and documents contained herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale of the Bonds will, under any circumstances, create any implication that the information contained herein has remained unchanged since the respective dates as of which such information is given herein.

**IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.**

*[Remainder of this page intentionally left blank.]*

## TABLE OF CONTENTS

## OFFICIAL STATEMENT SUMMARY

*This Summary, being part of the Official Statement, is subject in all respects to the more complete information contained therein. The offering of the Bonds to potential investors is made only by means of the entire Official Statement. No person is authorized to detach this Summary from the Official Statement or otherwise to use same without the entire Official Statement.*

| | |
|---|---|
| **Issuer** | Port of Houston Authority of Harris County, Texas, (the "Authority") a political subdivision of the State of Texas having boundaries coterminous with Harris County. |
| **Issue** | $36,665,000 "Port of Houston Authority of Harris County, Texas, Unlimited Tax Refunding Bonds, Series 2005A (AMT)" (the "Series 2005A Bonds") and $62,485,000 "Port of Houston Authority of Harris County, Texas, Unlimited Tax Refunding Bonds, Series 2005B (Non-AMT)" (the "Series 2005B Bonds") (collectively, the "Bonds"), each issued pursuant to the provisions of separate Orders (the "Orders"), adopted by the Commissioners Court of Harris County (the "Commissioners Court"), on behalf of the Authority. |
| **Use of Proceeds** | Proceeds of the Bonds will be used to refund all or a portion of the commercial paper notes of the Authority (the "Refunded Notes") and certain outstanding bonds of the Authority more particularly described in "APPENDIX E—Schedule of Refunded Bonds" (the "Refunded Bonds") and to pay costs of issuance. See "PLAN OF FINANCING." |
| **Payment Record** | The Authority has never defaulted in paying the principal of or interest on any of its bonds. |
| **Ratings** | See "RATINGS" herein. |
| **Amounts, Maturities, and Redemption** | The Bonds mature in the amounts shown on the inside cover page hereof on October 1 in each of the years 2012 through and including 2023. The Bonds are dated August 1, 2005, but bear interest from their date of delivery. The Bonds maturing on or after October 1, 2016 may be redeemed by the Authority before maturity in whole or, from time to time, in part, on October 1, 2015, or on any date thereafter, at the par value thereof plus accrued interest to the date fixed for redemption, upon 30 days written notice to the registered owners thereof. See "DESCRIPTION OF THE BONDS—Redemption" herein. |
| **Book-Entry-Only System** | The Bonds are initially issuable only to Cede & Co., as nominee for DTC, pursuant to a book-entry-only system. No physical delivery of the Bonds will be made to the beneficial owners of the Bonds. Principal and interest will be paid to Cede & Co., which will distribute such payment to the participating members of DTC for remittance to the beneficial owners of the Bonds. See "DESCRIPTION OF THE BONDS - Book-Entry-Only System" herein. The initial Paying Agent/Registrar for the Bonds is JPMorgan Chase Bank, National Association, Dallas, Texas. |
| **Interest Payment Dates** | Interest on the Bonds accrues from the date of delivery and is payable on April 1, 2006 and each April 1 and October 1 thereafter until the earlier of maturity or redemption, by check mailed to the registered owner of record as of the 15th day of the month next preceding each interest payment date. See "DESCRIPTION OF THE BONDS—General." |
| **Source of Payment** | Each series of the Bonds is payable from the receipts of a separate annual ad valorem tax, without legal limit as to rate, levied on taxable property within the Authority. See "DESCRIPTION OF THE BONDS—Source of Payment of the Bonds" and "AD VALOREM TAXES." |
| **Legal Investments and Eligibility to Secure Public Funds in Texas** | The Bonds are legal and authorized investments for banks, savings banks, trust companies, building and loan associations, savings and loan associations, insurance companies, fiduciaries, and trustees, and for the sinking funds of cities, towns, villages, school districts, and other political subdivisions or public agencies of the State of Texas. The "Public Funds Collateral Act," Chapter 2257, Texas Government Code, as amended, provides that deposits of public funds, as defined in such chapter, must be secured by eligible security. "Eligible Security" is defined to include a general or special obligation, payable from taxes, revenues, or a combination of taxes and revenues, issued by political subdivisions such as the Authority that have a current investment rating from a nationally recognized rating agency of not less than A, or its equivalent. See "LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS." |
| **Bond Insurance** | The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by MBIA Insurance Corporation. See "BOND INSURANCE" herein. |

## SELECTED AD VALOREM TAX DATA

**(dollar amounts in thousands)**

| | Tax Year | | | | |
|---|---|---|---|---|---|
| | 2004[a][b] | 2003 | 2002 | 2001 | 2000 |
| Total Assessed Value, Net of Exemptions[c] | $193,653,315 | $184,267,513 | $175,973,699 | $167,852,831 | $153,994, 369 |
| Ad Valorem Tax Rate (Per $100 of Assessed Value) | 0.01673 | 0.02000 | 0.01989 | 0.01826 | .01830 |
| Total Tax Levy | $32,398 | $36,923 | $34,904 | $30,659 | $28,191 |
| Current Collections of Ad Valorem Taxes Levied[d] | $30,932 | $34,417 | $32,558 | $28,574 | $26,144 |
| Current Collections as a Percentage of Ad Valorem Taxes Levied | 95.5% | 93.2% | 93.3% | 93.2% | 92.7 |
| Total Ad Valorem Collections[e] | $32,110 | $35,502 | $33,445 | $29,399 | $26,933 |
| Total Collections as a Percentage of Ad Valorem Taxes Levied | 99.1% | 96.2% | 95.8% | 95.9% | 95.5% |

| | Calendar Year | | | | |
|---|---|---|---|---|---|
| | 2004[a] | 2003 | 2002 | 2001 | 2000 |
| Authority Ad Valorem Tax Bonds Outstanding | $294,700 | $306,245 | $331,655 | $324,705 | $263,475 |
| Authority Ad Valorem Tax Bonds Outstanding as a Percentage of Assessed Value | 0.15% | 0.16% | 0.18% | 0.19% | 0.17% |

(a) Taxes levied in any year which are collected beginning October 1 of such year through June 30 of the following year are shown as current collections. Such amounts include that portion of the current levy collected on or after February 1, the date taxes become legally delinquent. See "AD VALOREM TAXES" herein.

(b) Such amounts include collections of delinquent taxes from prior years' levies of taxes collected during the period beginning on July 1 of the year shown and ending on June 30 of the following year.

(c) As of May 23, 2005.

(d) Taxes levied in any year which are collected beginning October 1 of such year through June 30 of the following year are shown as current collections. Such amounts include that portion of the current levy collected on or after February 1, the date taxes become legally delinquent. See "AD VALOREM TAXES" herein.

(e) Such amounts include collections of delinquent taxes from prior years' levies of taxes collected during the period beginning on July 1 of the year shown and ending on June 30 of the following year.

*Source: Harris County Tax Assessor-Collector.*

# OFFICIAL STATEMENT
# Relating to
# PORT OF HOUSTON AUTHORITY
# OF
# HARRIS COUNTY, TEXAS

**$36,665,000**
**UNLIMITED TAX REFUNDING BONDS,**
**SERIES 2005A (AMT)**

**$62,485,000**
**UNLIMITED TAX REFUNDING BONDS,**
**SERIES 2005B (NON-AMT)**

## INTRODUCTORY STATEMENT

This Official Statement is furnished in connection with the offering by the Port of Houston Authority of Harris County, Texas (the "Authority"), a political subdivision of the State of Texas (the "State"), having boundaries coterminous with Harris County, Texas (the "County"), of the above-captioned bonds (the "Series 2005A Bonds" and the "Series 2005B Bonds", and collectively, the "Bonds"). The Bonds of each series are issued pursuant to the provisions of separate orders adopted by the Commissioners Court of Harris County, Texas (the "Commissioners Court") on behalf of the Authority and separate orders adopted by the Authority (all such orders, collectively, the "Orders").

The Authority is a navigation district and a political subdivision of the State. The Authority owns and operates public wharves, docking facilities, freight handling facilities and related equipment, land, warehouses, railroad rights-of-way and trackage on the Houston Ship Channel (the "Houston Ship Channel" or the "Channel"). The Channel represents the heart of the Port of Houston ("Port") complex and extends 50 miles inland and links the City of Houston with the Gulf of Mexico. The Authority also owns and operates a channel and turning basin at the Bayport Industrial Complex near Houston. Because the Authority's boundaries are coterminous with those of the County, certain of the Authority's officials are also County officials. See "THE AUTHORITY" herein. Although the Bonds are issued pursuant to the provisions of the Orders adopted by the Commissioners Court, the Bonds are not obligations of the County. The Bonds are also not obligations of the City of Houston, Texas. See "DESCRIPTION OF THE BONDS—Source of Payment of the Bonds."

The Authority's financial statements, included in this Official Statement as APPENDIX A, present information on the general financial condition of the Authority at the dates and for the periods shown. The Bonds, however, are payable solely from the receipts of separate annual unlimited ad valorem taxes, and the inclusion of such statements and other financial information is not intended to imply that any other tax receipts, revenues, or moneys of the Authority are to be used to pay the principal of or interest on the Bonds. The Authority will also adopt two separate Orders (the "Authority Orders") authorizing the sale of the Bonds of each series, containing Continuing Disclosure Agreements and authorizing and approving certain other matters in connection with the issuance and delivery of the Bonds.

## PLAN OF FINANCING

### Refunded Notes

A portion of the proceeds of the Series 2005A Bonds will be used to refund the principal amount of $30,675,000 of the Authority's outstanding Port of Houston Authority of Harris County, Texas Unlimited Tax Commercial Paper Notes, Series A (AMT) and a portion of the proceeds of the Series 2005B Bonds will be used to refund the principal amount of $16,507,000 of the Authority's outstanding Port of Houston Authority of Harris County, Texas Unlimited Tax Commercial Paper Notes, Series A-1 (Non-AMT) (together, the "Refunded Notes"). The Authority will pay interest due on the Refunded Notes at maturity from other legally available funds. Proceeds of the Bonds and other legally available funds in an amount sufficient to accomplish the discharge and final payment of the Refunded Notes at maturity will be deposited with Deutsche Bank Trust Company Americas, the issuing and paying agent for the Refunded Notes.

**Refunding Bonds**

A portion of the proceeds of the Bonds will be used to refund a portion of the Authority's outstanding debt obligations as detailed and described in "APPENDIX E—Schedule of Refunded Bonds" (collectively, the "Refunded Bonds") (together with the Refunded Notes, the "Refunded Obligations"). The Refunded Bonds and interest due thereon will be paid on the scheduled interest payment, call or maturity dates of each such obligation, as the case may be, from funds to be deposited with JPMorgan Chase Bank, Dallas, Texas (the "Escrow Agent") to the Series 2005A Escrow Fund and the Series 2005B Escrow Fund, respectively, (together, the "Escrow Funds") created under two separate Escrow Agreements to be entered into by the Authority and the Escrow Agent for the Refunded Bonds (the "Escrow Agreements").

In addition to the Bonds, the Authority is contemplating the issuance of a series of forward refunding bonds in the approximate principal amount of $28,600,000 (the "2006A Bonds") which are anticipated to be delivered in July of 2006 to currently refund a portion of the Authority's Unlimited Tax Port Improvement Bonds, Series 1996. See "AUTHORITY AD VALOREM TAX DEBT – Possible Forward Refunding" herein.

The Orders and the Authority Orders for the Bonds will each provide that from the proceeds of the sale of the Bonds to the Underwriters, there will be deposited with the Escrow Agent the amount necessary to accomplish the discharge and final payment of the Refunded Bonds. Such funds will be held by the Escrow Agent in the Escrow Funds and will be used to purchase direct obligations of the United States of America (the "Federal Securities"). The Escrow Funds are irrevocably pledged to the payment of principal of and interest on the Refunded Bonds.

By the deposit of the Federal Securities and cash with the Escrow Agent pursuant to the Escrow Agreements, the Authority will have effected the defeasance of the Refunded Bonds, pursuant to the terms of the orders authorizing the Refunded Bonds and in accordance with applicable law, including Chapter 1207, Texas Government Code, as amended. It is the opinion of Bond Counsel that, as a result of such defeasance, the Refunded Bonds will no longer be payable from ad valorem taxes but will be payable solely from the principal of and interest on the Federal Securities and cash held for such purpose by the Escrow Agent, and that the Refunded Bonds will be defeased and are not to be included in or considered to be indebtedness of the Authority for the purpose of any limitation of indebtedness or taxation or for any other purpose.

The Authority has covenanted to make timely deposits into the Escrow Funds from lawfully available funds, of additional funds in the amounts required to pay the principal of and interest on the Refunded Bonds should, for any reason, the cash balances on deposit or scheduled to be on deposit in the Escrow Funds be insufficient to make such payments.

## SOURCES AND USES OF FUNDS

### Series 2005A Bonds

*The proceeds from the sale of the Series 2005A Bonds, will be applied approximately as follows:*

| | |
|---|---|
| Source of Funds: | |
| Principal Amount of the Series 2005A Bonds | $ 36,665,000.00 |
| Premium | 2,044,433.70 |
| Original Issue Discount | ( 205,586.40) |
| Total Sources of Funds | $38,503,847.30 |
| Uses: | |
| Deposit to Series 2005A Escrow Fund | $7,401,310.00 |
| Deposit to the Paying Agent/Registrar for the Refunded Notes | 30,675,000.00 |
| Costs of Issuance (including bond insurance) | 222,124.72 |
| Underwriters' Discount | 205,412.58 |
| Total Uses of Funds | $38,503,847.30 |

## Series 2005B Bonds

*The proceeds from the sale of the Series 2005B Bonds, will be applied approximately as follows:*

| | |
|---|---|
| Source of Funds: | |
| Principal Amount of the Series 2005B Bonds | $62,485,000.00 |
| Premium | 3,996,943.40 |
| Original Issue Discount | ( 211,620.00) |
| Total Sources of Funds | $66,270,323.40 |
| | |
| Uses: | |
| Deposit to Series 2005B Escrow Fund | $49,021,769.72 |
| Deposit to the Paying Agent/Registrar for the Refunded Notes | 16,507,000.00 |
| Costs of Issuance (including bond insurance) | 391,486.79 |
| Underwriters' Discount | 350,066.89 |
| Total Uses of Funds | $66,270,323.40 |

## DESCRIPTION OF THE BONDS

### General

The Bonds will be dated August 1, 2005, and will bear interest from the date of delivery at the per annum rates shown on the inside cover page hereof. Interest on the Bonds will be payable April 1 and October 1 of each year, commencing April 1, 2006, until maturity or earlier redemption, and will be payable by check mailed first class, postage prepaid on or before the interest payment date to the registered owners as of the 15th day of the month next preceding each interest payment date. The Bonds are issued only as fully-registered bonds in the denomination of $5,000 principal amount or any integral multiple thereof.

### Authority for the Bonds

The Bonds are issued pursuant to the provisions of the constitution and laws of the State of Texas, including particularly (i) Article XVI, Section 59 of the Texas Constitution, (ii) Chapter 117, Acts of the 55th Legislature, Regular Session, 1957, as amended, (iii) Chapter 1201, Texas Government Code, as amended, (iv) Chapter 1207, Texas Governmental Code, as amended, (v) Chapter 1371, Texas Government Code, as amended, and (vi) the Orders.

### Source of Payment of the Bonds

The Bonds are payable from the receipts of a separate annual ad valorem tax, unlimited as to rate, levied on taxable property within the County. See "AD VALOREM TAXES." Pursuant to the provisions of the Orders adopted at a regular meeting of the Commissioners Court, the Commissioners Court, on behalf of the Authority, has levied and agreed to assess and collect these annual ad valorem taxes. In each year the Commissioners Court, on behalf of the Authority, will determine the specific tax to be collected to pay interest as it accrues and principal as it matures on the Bonds of each series and will assess such taxes for that year. The receipts of such taxes are to be credited to separate funds to be used solely for the payment of the principal of and interest on the Bonds.

### Redemption

***Optional Redemption.*** The Bonds maturing on or after October 1, 2016 are subject to redemption at the option of the Authority, as a whole or from time to time in part in integral multiples of $5,000 principal amount on any date on or after October 1, 2015, upon payment of a redemption price equal to 100% of the principal amount thereof, plus accrued interest on the Bonds called for redemption from the most recent interest payment date to the redemption date.

***Method of Selecting Bonds to be Redeemed.*** If less than all of the Bonds of each series are to be redeemed, the Authority may select the maturity or maturities to be redeemed. If less than all of the Bonds of a series of any maturity are to be redeemed, the particular Bonds or portions thereof to be redeemed will be selected by lot or other random method in integral multiples of $5,000. In selecting for redemption portions of Bonds in denominations larger than $5,000, each such Bond will be treated as representing that number of Bonds of $5,000 denomination that is obtained by dividing the principal amount of such Bond by $5,000.

***Notice of Redemption.*** Any notice of redemption identifying the series of the Bonds or portions thereof to be redeemed will be sent to the registered owners thereof by first class mail not less than 30 days prior to the date fixed for redemption, but neither the failure to give such notice nor any defect therein will affect the sufficiency of notice given to Bondholders.

***Partial Redemption.*** Any Bond which is to be redeemed only in part will be surrendered to the Paying Agent/Registrar (with, if the Authority or the Paying Agent/Registrar so requires, due endorsement by, or written instrument of transfer in form satisfactory to the Authority and the Paying Agent/Registrar duly executed by, the holder thereof or such holder's authorized representative), and the Authority will execute and the Paying Agent/Registrar will authenticate and deliver to the holder of such a new Bond or Bonds of the same series and maturity and of any authorized denomination or denominations as requested by such holder in aggregate principal amount equal to and in exchange for the unredeemed portion of the principal of the Bond so surrendered.

**Book-Entry-Only System**

*Appendix B describes how ownership of the Bonds is to be transferred and how the principal of, premium, if any, and interest on the Bonds are to be paid to and credited by DTC while the Bonds are registered in its nominee name. The information in Appendix B concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The Authority believes the source of such information to be reliable, but takes no responsibility for the accuracy or completeness thereof.*

*The Authority cannot and does not give any assurance that (1) DTC will distribute payments of debt service on the Bonds, or other notices, to DTC Participants, (2) DTC Participants or others will distribute debt service payments paid to DTC or its nominee (as the registered owner of the Bonds), or other notices, to the Beneficial Owners, or that they will do so on a timely basis, or (3) DTC will serve and act in the manner described in this Official Statement. The current rules applicable to DTC are on file with the Securities and Exchange Commission, and the current procedures of DTC to be followed in dealing with DTC Participants are on file with DTC.*

*DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee). One fully-registered certificate will be issued for each maturity of the Bonds in the aggregate principal amount of each such maturity and will be deposited with DTC.*

***Use of Certain Terms in Other Sections of this Official Statement.*** In reading this Official Statement it should be understood that while the Bonds are in the Book-Entry-Only System, references in other sections of this Official Statement to registered owners should be read to include the person for which the Participant acquires an interest in the Bonds, but (i) all rights of ownership must be exercised through DTC and the Book-Entry-Only System, and (ii) except as described above, notices that are to be given to registered owners under the Orders will be given only to DTC.

Information concerning DTC and the Book-Entry-Only System has been obtained from DTC and is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the Authority or the Underwriters.

**Ownership**

The Authority, the Paying Agent/Registrar and any agent of either may treat the person in whose name any Bond is registered as the absolute owner of such Bond for the purpose of making and receiving payment of the principal and redemption price thereof, and for the further purpose of making and receiving payment of the interest thereon, and for all other purposes. Neither the Authority, the Paying Agent/Registrar, nor any agent of either of them will be bound by any notice or knowledge to the contrary. All payments made to the person deemed to be the owner of any Bond in accordance with the Orders and the issuance of such Bonds will be valid and effective and will discharge the liabilities of the Authority and the Paying Agent/Registrar for such Bond to the extent of the sums paid.

**Transfers and Exchanges**

A bond register relating to the registration, payment, and transfer or exchange of the Bonds of each series (the "Bond Register") will be kept and maintained by the Authority, at the corporate trust office of the Paying Agent/Registrar, as provided in the Orders authorizing the issuance of such series of the Bonds and in accordance with the provisions of an agreement with the Paying Agent/Registrar and such rules and regulations as the Paying Agent/Registrar and the Authority may prescribe.

Whenever the Paying Agent/Registrar is a banking or trust corporation or association not domiciled in the State, the Authority will cause the Paying Agent/Registrar to keep a copy of the Bond Register with the Authority in the Authority's offices in Houston, Texas. Any Bond may be transferred or exchanged for Bonds of other authorized denominations (within the maturity) and of like aggregate principal amount and series by the registered owner, in person or by its duly authorized agent, upon surrender of such Bonds to the Paying Agent/Registrar for cancellation, accompanied by a written instrument of transfer or request for exchange duly executed by the registered owner or by his duly authorized agent, in form satisfactory to the Paying Agent/Registrar.

Upon surrender of any Bonds for transfer at the corporate trust office of the Paying Agent/Registrar, the Authority will execute and the Paying Agent/Registrar will register and deliver, in the name of the designated transferee or transferees, one or more new Bonds of authorized denominations (within the same maturity) and of like series, aggregate principal amount, and maturity as the Bond or Bonds surrendered for transfer.

At the option of the registered owner, Bonds may be exchanged for other Bonds of authorized denominations (within the same maturity and series) and of like aggregate principal amount (less, in the case of partial redemption thereof, the amount so redeemed) as the Bonds surrendered for exchange, upon surrender of the Bonds to be exchanged at the corporate trust office of the Paying Agent/Registrar.

All Bonds issued in any transfer or exchange of Bonds will be delivered to the registered owners and upon the registration and delivery thereof, the same will be the valid obligations of the Authority evidencing the same obligation to pay, and entitled to the same benefits under the Orders authorizing the issuance of such Bonds, as the Bonds surrendered in such transfer or exchange.

All transfers or exchanges of Bonds pursuant to the Orders authorizing the issuance of such Bonds will be made without expense or service charge to the registered owner, except that the Paying Agent/Registrar will require payment by the registered owner requesting such transfer or exchange of any tax or other governmental charges required to be paid with respect to such transfer or exchange.

**Amendments**

The Commissioners Court, on behalf of the Authority, may, without the consent of or notice to any bondholder, from time to time and at any time, amend the Orders in any manner not detrimental to the interest of the bondholders, including the curing of any ambiguity, inconsistency or formal defect or omission therein. In addition, the Commissioners Court, on behalf of the Authority, may, with the written consent of bondholders holding a majority in aggregate principal amount of the Bonds then outstanding affected thereby and the bond insurer, if any, amend, add to or rescind any of the provisions of the Orders, provided that, without the consent of all bondholders of outstanding Bonds affected thereby and the bond insurer, if any, no such amendment, addition or rescission will (1) change the maturity of such Bonds or any Interest Payment Date for an installment of interest thereon, reduce the principal amount thereof or the rate or interest thereon, change the places at, or the coin or currency in, which any such Bond or the interest thereon is payable or in any other way modify the terms of payment of the principal of or interest on such Bonds, (2) give any preference to any such Bond over any other such Bond, or (3) reduce the aggregate principal amount of Bonds required to consent to any such amendment, addition or rescission, except to increase the percentage provided thereby or to provide that certain other provisions of the Orders cannot be modified or waived without the consent of the owners of the Bonds of the related series and the bond insurer, if any.

**Defeasance**

The provisions of the Orders and the obligations to the Registered Owners of any or all of the Bonds to pay the principal of and interest thereon may be defeased in any manner permitted by law, including by depositing with the Paying Agent/Registrar, the Comptroller of Public Accounts of the State of Texas or any other entity with which such deposits may be made (as specified by Section 1207.061, Texas Government Code, as amended) either: (a) cash in an amount equal to the principal amount of such Bonds plus interest thereon to the date of maturity or redemption, or (b) pursuant to an escrow or trust agreement (or, if payment or redemption will occur on or before the next Interest Payment Date, by deposit to the debt service fund for the Bonds), cash and/or:

(1) direct noncallable obligations of the United States, including obligations that are unconditionally guaranteed by the United States;

(2) noncallable obligations of an agency or instrumentality of the United States, including obligations that are unconditionally guaranteed or insured by the agency or instrumentality and that, on the date the Commissioners Court adopts or approves the proceedings authorizing the issuance of refunding bonds, are rated as to investment quality by a nationally recognized investment rating firm not less than "AAA" or its equivalent;

(3) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that, on the date the Commissioners Court adopts or approves the proceedings authorizing the issuance of refunding bonds, are rated as to investment quality by a nationally recognized investment rating firm not less than "AAA" or its equivalent; and/or

(4) any other securities or obligations which, at the time of such defeasance, are authorized by state law to be used to effectuate a defeasance of the Bonds,

in principal amounts and maturities and bearing interest at rates sufficient to provide for the timely payment of the principal amount of the Bonds plus interest thereon to the date of maturity or redemption; provided, however, that if any of the Bonds are to be redeemed prior to their respective dates of maturity, provision will have been made for giving notice of redemption as provided in the Orders. Upon such deposit, such Bonds will no longer be regarded to be Outstanding or unpaid.

## AD VALOREM TAXES

The Commissioners Court is responsible for levying taxes on behalf of the Authority. While the Authority's rates of taxation differ from the County's, the procedures for assessing, levying and collecting tax are, except as otherwise described below, substantially the same as those followed by the County.

### Property Subject to Taxation

Except for certain exemptions provided by State law, all real and certain tangible personal property and certain intangible personal property with a tax situs in the County is subject to taxation by the County. The County's assessed value, less the assessed value of the rolling stock of railroads and intangible properties of railroads and certain common carriers, is the assessed value used by the Commissioners Court to determine the tax rate for the Authority's levy. Principal categories of exempt property include: property owned by the State or its political subdivisions if the property is used for public purposes; property exempt from ad valorem taxation by federal law; certain improvements to real property and certain tangible personal property, located in designated reinvestment zones, on which ad valorem taxes have been abated for a specified period of time pursuant to tax abatement agreements; farm products owned by the producer; certain property owned by qualified charitable, religious, veterans, youth, fraternal or educational organizations; property of a nonprofit corporation that is used in scientific research and educational activities benefiting a college or university; designated historic sites; solar and wind powered energy devices; nonprofit cemeteries; and tangible personal property not held or used for production of income.

### Valuation of Property for Taxation

The Property Tax Code of Texas (the "Property Tax Code") generally requires all taxable property (except property utilized for a qualified "agricultural use," as that definition has been expanded by recent legislation, and timberland) to be appraised at 100% of market value as of January 1 of each year. Residential property that has never been occupied as a residence and is being held for sale is treated as inventory for property tax purposes. The appraisal of taxable property for the County (including certain railroad rolling stock and certain intangible property of railroads and certain common carriers, which still is appraised by the State) and all other taxing entities in the

County, including the Authority, is the responsibility of the Harris County Appraisal District (the "Appraisal District"), a county-wide agency created under the Property Tax Code for that purpose.

The Appraisal District is governed by a five-member board whose members are appointed by vote of the Commissioners Court and the governing bodies of the cities, towns, school districts and, upon request, conservation and reclamation districts in the County under a voting system weighted in direct proportion to the amount of taxes imposed by the voting entities. Cumulative voting for Appraisal District Board members is permitted, and, through the exercise of that right, the Commissioners Court, the Houston City Council and the Houston Independent School District Board of Education may each select one member.

The Property Tax Code requires the Appraisal District to implement a plan for periodic reappraisal of all taxable property in the County, and reappraisal must be effected at least once every three years. The Appraisal District has established a schedule of reappraisal for different classifications of property to comply with such requirements.

Taxable values determined by the chief appraiser of the Appraisal District are submitted for review and equalization to an Appraisal Review Board, (the "Appraisal Review Board") appointed by the Appraisal District. Appraisals may be contested before the Appraisal Review Board by taxpayers or, under limited circumstances, the County, and the Appraisal Review Board's orders are appealable to a State district court.

**Limitations on Tax Rate Increases**

The Commissioners Court is required to set its tax rate before the later of September 30 or the 60th day after the certified appraisal roll is received by the County. If the Commissioners Court does not adopt a tax rate before the required date, the tax rate for the County is the lower of the effective tax rate calculated for that tax year or the tax rate adopted by the County for the preceding tax year. Such rates are based on the assessed values at January 1 of each year, as shown on the tax roll approved by the Appraisal Review Board, which must be used by the County for such purpose. The Tax Code imposes limitations on certain tax increases. The Commissioners Court may under certain circumstances be required to publish notice and hold a public hearing on a proposed tax rate before voting on the tax rate. If the tax rate adopted exceeds by more than 8% the rate needed to pay debt service and certain contractual bonds, and to produce, when applied to the property which was on the prior year's roll, the prior year's taxes levied for purposes other than debt service and such contractual bonds, such excess portion of the levy may be repealed at an election within the County held upon petition of 10% of the qualified voters of the County.

**Collections, Penalty and Interest**

The County Tax Assessor-Collector is responsible for collection of taxes. Tax statements are required to be mailed by September 1, or as soon thereafter as practicable, and taxes become delinquent on February 1 of the following year. If tax statements are mailed after January 10, the delinquency date is postponed to the first day of the next month that will provide a period of at least 21 days between the date the statement is mailed and the date taxes become delinquent. So long as the Commissioners Court or voters of the County have not transferred responsibility for collection of the taxes to another taxing unit as described above, the County may permit payment without penalty or interest of one-half of the taxes due from each taxpayer by July 1 if one-half of the taxes due for the current year from such taxpayers are paid prior to December 1. Delinquent taxes are subject to a 6% penalty for the first month of delinquency, 1% for each month thereafter to July 1, and 12% total if any taxes are unpaid on July 1. Delinquent taxes also accrue interest at the rate of 1% per month during the period they remain outstanding. If the delinquency date is postponed, then the postponed date is the date from which penalty and interest accrue on the delinquent taxes. The County may impose an additional penalty for collection costs for certain delinquent taxes if the County has contracted with a collection attorney. The County may waive penalties and interest on delinquent taxes if the error or omission of a representative of the County or of the Appraisal District, as applicable, caused the failure to pay the tax before delinquency and if the tax is paid within 21 days after the taxpayer knows or should know of the delinquency.

**Tax Liens**

The Property Tax Code provides that on January 1 of each year a tax lien attaches to property to secure the payment of all taxes, penalties and interest ultimately imposed for the year on the property. The lien exists in favor of each taxing unit, including the Authority, having power to tax the property. The tax lien on real property has priority over the claims of most creditors and other holders of liens on the property encumbered by the tax lien, whether or not the other debt or lien existed before the attachment of the tax lien. Taxes levied by the County are the personal obligation of the property owner and, under certain circumstances, personal property is subject to seizure and sale for the payment of delinquent taxes, penalty and interest thereon. Except with respect to taxpayers 65 and older, any time after taxes on property become delinquent, the Authority may file suit to foreclose the lien securing payment of the tax, to enforce personal liability for the tax or both. In filing a suit to foreclose a tax lien on real property, the Authority must join other taxing units that have claims for delinquent taxes against all or part of the same property. The ability of the Authority to collect delinquent taxes by foreclosure may be adversely affected by the amount of taxes owed to other taxing units, certain affirmative defenses, adverse market conditions affecting the liquidation of such property, taxpayer redemption rights, general principles of equity or bankruptcy proceedings that restrain the collection of a taxpayer's debt.

Federal bankruptcy law provides that an automatic stay of actions by creditors and other entities, including governmental units, goes into effect with the filing of any petition in bankruptcy. The automatic stay prevents governmental units from foreclosing on property and prevents enforcement of liens for post-petition taxes from the bankruptcy court. In many cases post-petition taxes are paid as an administrative expense of the estate in bankruptcy or by order of the bankruptcy court.

## AUTHORITY AD VALOREM TAXES

### Table 1 - Table of Authority Tax Rates

The following table shows the ad valorem tax rates per $100 of assessed value levied by the County on behalf of the Authority, for each of the tax years 2000 through 2004 The table does not show the ad valorem tax rates levied by other County-wide taxing entities. See "AUTHORITY AD VALOREM TAXES—County-Wide Ad Valorem Tax Rates." The tax year of the Authority is the calendar year. The ad valorem tax rate that the Commissioners Court may levy on behalf of the Authority to pay the Authority's tax bonds is unlimited.

| Purpose | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|
| Debt Service | $0.01830 | $0.01826 | $0.01989 | $0.02000 | $0.01673 |

*[Remainder of this page intentionally left blank]*

**Table 2 - Table of Authority Taxable Values and Tax Rates**

The following table shows the Authority's taxable values and tax rates for each of the tax years 2000 through 2004. Taxable property is assessed at 100% of the appraised value as established by the Appraisal District.

**Assessed Value as of January 1**
(dollar amounts in thousands)

| | Taxable Value as of January 1 | | | |
|---|---|---|---|---|
| Tax Year | Real Property[a][b] | Personal Property | Total[a][b][c] | Authority Tax Rate per $100 of Taxable Value |
| 2000 | $125,699,404 | $28,397,625 | $154,097,029 | $0.01830 |
| 2001 | 138,032,592 | 29,631,016 | 167,663,608 | 0.01826 |
| 2002 | 145,787,868 | 30,171,225 | 175,959,093 | 0.01989 |
| 2003 | 141,948,268 | 33,764,699 | 175,712,967 | 0.02000 |
| 2004 | 161,904,618 | 31,748,697 | 193,653,315[d] | 0.01673 |

(a) Net of exemptions and abatements.

(b) The County, either by action of the Commissioners Court or through a process of petition and referendum initiated by its residents, may grant partial exemptions for residential homesteads of persons 65 years or older and of certain disabled persons. The Commissioners Court granted an exemption for residential homesteads for persons 65 years of age or older and disabled persons of up to $156,240 of assessed value for 2004. If requested, the County must grant exemptions to disabled veterans or certain surviving dependents of disabled veterans or of persons who died while on active duty in an amount not to exceed $3,000 of assessed value. The County may also authorize exemptions of up to 20% of the value of residential homesteads from ad valorem taxation. The Commissioners Court granted a 20% exemption for 2004. Counties may also refrain from increasing the total ad valorem tax (except for increases attributable to certain improvements on residential homesteads) of disabled persons or persons 65 years of age or older and their spouses above the amount of tax imposed in the later of (1) the year such residence qualified for an exemption based on the disability or age of the owner or (2) the year such county chooses to establish such limitation. The County has not chosen to institute such tax freeze. If ad valorem taxes have been pledged for the payment of debt prior to the adoption of any such partial exemptions, taxes may be assessed and collected against the exempt value of such homesteads if the cessation of the levy against such exempt value would impair the obligation of the contract by which the debt was created.

(c) The County and certain taxing units located within the County may enter into tax abatement agreements to encourage economic development. Under such agreements, a property owner agrees to construct certain improvements on its property. The County or taxing unit (as applicable) in turn agrees not to levy a tax on all or part of the increased value attributable to the improvements until the expiration of the agreement. Any such abatement agreement may last for a period of up to 10 years. If the County or taxing unit (as applicable) enters into a tax abatement agreement with owners of taxable property within the Authority, the Authority must abate taxes on the improvements in the same manner as the County or taxing unit. The estimated value of property in the County that was subject to tax abatement as of May 23, 2005 was approximately $1.3 billion and such value at the end of the abatement period is currently estimated to be approximately $1.9 billion. Taxable value figures herein are net of abatements.

(d) Estimates based on Appraisal District tax supplement as of May 23, 2005

*Source: Harris County Tax Assessor-Collector.*

*[Remainder of this page intentionally left blank]*

**Table 3 - Table of Authority Tax Levies, Collections, and Delinquencies**

The table below sets forth a comparison of the ad valorem taxes levied and collected by the County on behalf of the Authority for the tax years 2000 through 2004.

(dollar amounts in thousands)

| Year | Total Tax Levy | Current Tax Collections[a] | Percent of Current Levy | Delinquent Collections[b] | Total Tax Collections | Percent of Total Collections to Levy | Delinquent Taxes Receivable[b] Personal Property | Delinquent Taxes Receivable[b] Real Property |
|---|---|---|---|---|---|---|---|---|
| 2000 | $28,191 | $26,144 | 92.7% | $ 789 | $26,933 | 95.5% | $ 869 | $1,635 |
| 2001 | 30,659 | 28,574 | 93.2 | 825 | 29,399 | 95.9 | 1,046 | 1,730 |
| 2002 | 34,904 | 32,558 | 93.3 | 887 | 33,445 | 95.8 | 1,091 | 1,770 |
| 2003 | 36,923 | 34,417 | 93.2 | 1,085 | 35,502 | 96.2 | 1,213 | 1,836 |
| 2004[c] | 32,398 | 30,932 | 95.5 | 1,178 | 32,110 | 99.1 | 1,255 | 1,782 |

(a) Taxes levied in any year that are collected beginning October 1 of such year through June 30 of the following year are shown as current collections. Such amounts include that portion of the current levy collected on or after February 1, which is the date taxes become legally delinquent.

(b) Collections of prior years' levies of taxes during the period beginning July 1 of the year shown and ending on June 30 of the following year are shown as delinquent collections. The accumulation of all unpaid ad valorem taxes that were due at the end of the collection period beginning on July 1 of the year shown and ending on June 30 of the following year is shown as delinquent taxes receivable. The Authority is barred from bringing suit for collection of delinquent personal property taxes after four years from the time such taxes become delinquent. Real property taxes, until paid, constitute a lien against the property. The Authority is barred from bringing suit for collection of delinquent real property taxes after 20 years from the time such taxes become delinquent. The Authority writes off such uncollectable personal property and real property taxes annually. Pursuant to Section 33.05, subsection (c) of the Property Tax Code, the County Tax Assessor-Collector is required to cancel and remove from the delinquent tax roll a tax on real property that has been delinquent for more than 20 years or a tax on personal property that has been delinquent for more than 10 years. The delinquent taxes may not be canceled if litigation concerning the taxes is pending.

(c) As of May 23, 2005.

*Source: Harris County Tax Assessor-Collector.*

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**Table 4 - Table of Principal Taxpayers**

The following table lists the 15 taxpayers with the largest taxable values in the Authority as of January 1, 2004:

(dollar amounts in thousands)

| Taxpayers | Type of Business | 2004 Taxable Valuations[(a)] | Percentage of Total 2004 Taxable Valuation[(b)] |
|---|---|---|---|
| Exxon Mobil Corporation | Oil, Chemical Plant | $ 2,887,139 | 1.49% |
| Centerpoint Energy Inc. | Electric Utility | 2,325,222 | 1.20 |
| Shell Oil Company | Oil Refinery | 1,421,282 | 0.73 |
| SBC Communications Inc. | Telephone Utility | 1,009,651 | 0.52 |
| Equistar Chemicals Ltd. Partnership | Chemical | 976,266 | 0.50 |
| Hines Interests Ltd. Partnership | Real Estate | 867,174 | 0.45 |
| Chevron Phillips Chemical Company | Oil, Chemical Plant | 598,246 | 0.31 |
| Lyondell Chemical | Oil, Chemical Plant | 582,262 | 0.30 |
| Anheuser Busch Inc. | Brewery | 482,235 | 0.25 |
| Crescent Real Estate | Real Estate | 441,402 | 0.23 |
| Oxy Vinyls LP | Oil, Chemical Plant | 383,015 | 0.20 |
| Lyondell-Citgo Refining Co. | Oil, Refinery | 356,395 | 0.18 |
| Continental Airlines Inc. | Airline | 351,538 | 0.18 |
| Hewlett Packard Company. | Computers | 346,036 | 0.18 |
| Rohm and Haas Co. | Chemical | 333,377 | 0.17 |
| **Total** | | $13,361,240 | 6.89% |

(a) Amounts shown for these taxpayers do not include taxable valuations, which may be substantial, attributable to certain subsidiaries and affiliates which are not grouped on the tax rolls with the taxpayers shown.

(b) Based on the County's total taxable value as of February 1, 2005.

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### County-Wide Ad Valorem Tax Rates

In addition to the Authority's ad valorem taxes, the Commissioners Court levies taxes on property in the County on behalf of the County, the Harris County Flood Control District and the Harris County Hospital District. As with the Authority, the County Tax Assessor-Collector collects ad valorem taxes for the Harris County Flood Control District and the Harris County Hospital District using the same property values as the County, except that the rolling stock of railroads and intangible properties of railroads and certain common carriers are taxable only by the County.

### Table of County-Wide Ad Valorem Tax Rates

The following table shows the ad valorem tax rates per $100 of assessed value levied by the County for each of the tax years 2000 through 2004. The tax rates are based on assessment of taxable property at 100% of appraised value. (The tax year of the County is the calendar year, but its fiscal year begins March 1 and ends on the last day of February of the next year.) The County Tax Assessor-Collector collects ad valorem taxes for the Harris County Flood Control District, the Authority and the Harris County Hospital District using the same property values as the County, except that the rolling stock of railroads and intangible properties of railroads and certain common carriers are taxable only by the County.

| | Tax Years | | | | |
|---|---|---|---|---|---|
| **Purpose** | **2000** | **2001** | **2002** | **2003** | **2004** |
| County: | | | | | |
| Operating Fund | $0.32599 | $0.33606 | $0.33538 | $0.34490 | $0.33117 |
| Debt Service | 0.01772 | 0.02368 | 0.03056 | 0.01889 | 0.04303 |
| Total ($0.80 Limited Tax Rate) | 0.34371 | 0.35974 | 0.36594 | 0.36379 | 0.37420 |
| Road Bond Debt Service: | | | | | |
| (Unlimited Tax Rate) | 0.01531 | 0.02419 | 0.02220 | 0.02424 | 0.02566 |
| Toll Road Authority Tax Bond: | | | | | |
| Debt Service (Unlimited Tax Rate)[(a)] | -- | -- | -- | -- | -- |
| Total County Tax Rate | $0.35902 | $0.38393 | $0.38814 | $0.38803 | $0.39986 |
| Harris County Flood Control District[(b)] | $0.06173 | $0.04758 | $0.04174 | $0.04174 | $0.03318 |
| Port of Houston Authority Debt Service[(c)] | 0.01830 | 0.01826 | 0.01989 | 0.02000 | 0.01673 |
| Harris County Hospital District[(d)] | 0.20268 | 0.19021 | 0.19021 | 0.19021 | 0.19021 |
| Total County-Wide Ad Valorem Tax Rate | $0.64173 | $0.63998 | $0.63998 | $0.63998 | $0.63998 |

(a) The County's policy and practice has been to provide for payment of debt service on the Toll Road Authority Tax Bond debt from toll revenues and certain other funds, and no taxes have to date been collected to provide for such debt service.

(b) The ad valorem tax rate that the Commissioners Court may levy on behalf of the Harris County Flood Control District is limited by law to a maximum of $0.30 per $100 of assessed value.

(c) The ad valorem tax rate that the Commissioners Court may levy on behalf of the Authority to pay the Authority's tax bonds is by law unlimited.

(d) The ad valorem tax rate that the Commissioners Court may levy on behalf of the Harris County Hospital District is limited by law to a maximum of $0.75 per $100 assessed value.

*Source: Harris County Tax Assessor-Collector.*

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## AUTHORITY AD VALOREM TAX DEBT

### Payment Record

The Authority has never defaulted in the payment of the principal of or the interest on any of its bonds.

### Table 5 - Table of Ad Valorem Tax Debt Comparisons

The following table sets forth the Authority's ad valorem tax debt outstanding, as of the end of the fiscal years ended December 31, 2000, through December 31, 2004, as a percentage of taxable value and per capita.

| Fiscal Year End | Authority's Debt Outstanding (in thousands) | Authority's Taxable Value[a] (in thousands) | Authority's Debt Outstanding as a Percentage of Taxable Value | Estimated Population | Authority's Tax Debt Outstanding Per Capita |
|---|---|---|---|---|---|
| 2000 | $263,475 | $153,619,037 | 0.17% | 3,400,578 | $77 |
| 2001 | 324,705 | 167,852,831 | 0.19 | 3,460,589 | 94 |
| 2002 | 331,655 | 175,973,699 | 0.19 | 3,557,055 | 93 |
| 2003 | 306,245 | 184,267,513 | 0.17 | 3,596,086 | 85 |
| 2004 | 294,700 | 193,653,315[b] | 0.15 | 3,644,285[c] | 81 |

(a) Net of exemptions and abatements. Property is assessed at 100% of appraised value.
(b) Estimated as of May 23, 2005.
(c) Source: U.S. Census Bureau at July 1, 2004
*Source: Harris County Appraisal District.*

*[Remainder of this page intentionally left blank.]*

**Table 6 - Table of Debt Service Requirements**

The following table sets forth the annual debt service requirements on the Authority's outstanding ad valorem tax bonds adjusted to include the Bonds and excluding the Refunded Bonds.

| Fiscal Year Ending 12/31 | Outstanding Debt Service Requirements | Refunded Debt Service Requirements | Series 2005A Bonds Principal | Series 2005A Bonds Interest | Series 2005A Bonds Total | Series 2005B Bonds Principal | Series 2005B Bonds Interest | Series 2005B Bonds Total | Total Outstanding Debt Service Requirements [(a)] |
|---|---|---|---|---|---|---|---|---|---|
| 2005 | $ 33,260,283 | $ 1,415,958 | $ - | $ - | $ - | $ - | $ - | $ - | $ 31,844,325 |
| 2006 | 32,414,433 | 5,916,915 | - | 1,867,471 | 1,867,471 | - | 3,241,403 | 3,241,403 | 31,606,392 |
| 2007 | 31,557,045 | 5,789,290 | - | 1,755,325 | 1,755,325 | - | 3,046,750 | 3,046,750 | 30,569,830 |
| 2008 | 30,675,578 | 5,666,960 | - | 1,755,325 | 1,755,325 | - | 3,046,750 | 3,046,750 | 29,810,693 |
| 2009 | 29,811,193 | 5,550,985 | - | 1,755,325 | 1,755,325 | - | 3,046,750 | 3,046,750 | 29,062,283 |
| 2010 | 26,997,824 | 5,434,710 | - | 1,755,325 | 1,755,325 | - | 3,046,750 | 3,046,750 | 26,365,189 |
| 2011 | 25,376,705 | 5,312,010 | - | 1,755,325 | 1,755,325 | - | 3,046,750 | 3,046,750 | 24,866,770 |
| 2012 | 23,819,680 | 5,196,985 | - | 1,755,325 | 1,755,325 | 1,815,000 | 3,046,750 | 4,861,750 | 25,239,770 |
| 2013 | 23,245,150 | 5,071,485 | - | 1,755,325 | 1,755,325 | 2,355,000 | 2,956,000 | 5,311,000 | 25,239,990 |
| 2014 | 21,674,910 | 4,947,510 | 3,920,000 | 1,755,325 | 5,675,325 | - | 2,838,250 | 2,838,250 | 25,240,975 |
| 2015 | 21,143,880 | 4,819,950 | 4,515,000 | 1,559,325 | 6,074,325 | - | 2,838,250 | 2,838,250 | 25,236,505 |
| 2016 | 20,622,605 | 4,698,313 | 5,145,000 | 1,333,575 | 6,478,575 | - | 2,838,250 | 2,838,250 | 25,241,118 |
| 2017 | 19,421,468 | 4,574,575 | 6,480,000 | 1,076,325 | 7,556,325 | -- | 2,838,250 | 2,838,250 | 25,241,468 |
| 2018 | 15,740,318 | 3,854,363 | 9,695,000 | 817,125 | 10,512,125 | - | 2,838,250 | 2,838,250 | 25,236,330 |
| 2019 | 14,045,183 | 2,364,175 | 5,160,000 | 332,375 | 5,492,375 | 5,230,000 | 2,838,250 | 8,068,250 | 25,241,633 |
| 2020 | 9,422,520 | 2,001,525 | - | 74,375 | 74,375 | 15,165,000 | 2,576,750 | 17,741,750 | 25,237,120 |
| 2021 | 9,436,430 | 2,004,125 | - | 74,375 | 74,375 | 15,915,000 | 1,818,500 | 17,733,500 | 25,240,180 |
| 2022 | 9,451,968 | 1,998,413 | - | 74,375 | 74,375 | 16,005,000 | 1,022,750 | 17,027,750 | 24,555,680 |
| 2023 | 9,474,018 | 2,002,913 | 1,750,000 | - | 1,824,375 | 6,000,000 | 247,500 | 6,247,500 | 15,542,980 |
| 2024 | 9,494,710 | 2,001,775 | - | - | - | - | - | - | 7,492,935 |
| 2025 | 7,513,035 | - | - | - | - | - | - | - | 7,513,035 |
| 2026 | 7,535,645 | - | - | - | - | - | - | - | 7,535,645 |
| 2027 | 1,149,750 | - | - | - | - | - | - | - | 1,149,750 |
| Total | $433,284,331 | $80,622,933 | $36,665,000 | $21,326,296 | $57,991,296 | $62,485,000 | $47,172,904 | $109,657,904 | $520,310,594 |

(a) Discrepancies in totals due to rounding.
*Source: First Southwest Company.*

**Table of County-Wide Ad Valorem Tax Debt Service Requirements**

The following table sets forth the debt service requirements on County-wide outstanding ad valorem tax debt as of July 1, 2005, excluding commercial paper. See "—Commercial Paper." The following table includes the debt service on the Bonds and excludes the future debt service payment on the Refunded Obligations.

| Fiscal Year (End of Feb.) | County Limited Tax Bonds | County Unlimited Tax Bonds | Toll Road Unlimited Tax Bonds[a] | Flood Control District Limited Tax Bonds[b] | Port of Houston Authority Unlimited Tax Bonds | Total[c] |
|---|---|---|---|---|---|---|
| 2006[d] | $ 76,204,422 | $ 51,532,021 | $ 75,453,269 | $ 38,070,412 | $ 31,844,325 | $ 273,104,449 |
| 2007 | 76,172,199 | 52,769,018 | 75,413,269 | 35,127,524 | 31,606,392 | 271,088,402 |
| 2008 | 74,627,994 | 54,298,124 | 74,863,269 | 34,437,744 | 30,569,830 | 268,796,961 |
| 2009 | 76,883,994 | 52,027,737 | 74,988,031 | 30,846,244 | 29,810,693 | 264,556,699 |
| 2010 | 77,673,211 | 51,795,937 | 87,220,694 | 30,130,144 | 29,062,283 | 275,882,269 |
| 2011 | 73,363,211 | 56,403,362 | 86,496,694 | 27,728,631 | 26,365,189 | 270,357,087 |
| 2012 | 78,972,215 | 50,765,987 | 85,577,444 | 25,418,256 | 24,866,770 | 265,600,672 |
| 2013 | 81,928,303 | 46,509,577 | 85,312,031 | 25,206,706 | 25,239,770 | 264,196,387 |
| 2014 | 77,221,753 | 49,241,804 | 85,105,613 | 25,014,981 | 25,239,990 | 261,824,141 |
| 2015 | 78,987,548 | 47,536,904 | 84,494,981 | 23,497,644 | 25,240,975 | 259,758,052 |
| 2016 | 79,556,880 | 46,958,666 | 60,148,275 | 22,328,275 | 25,236,505 | 234,228,601 |
| 2017 | 80,600,863 | 45,932,116 | 44,204,397 | 21,147,513 | 25,241,118 | 217,126,007 |
| 2018 | 80,470,193 | 45,925,078 | 43,639,441 | 21,146,088 | 25,241,468 | 216,422,268 |
| 2019 | 65,602,370 | 45,928,553 | 43,062,831 | 36,129,975 | 25,236,330 | 215,960,059 |
| 2020 | 50,482,065 | 45,929,997 | 42,471,594 | 51,326,413 | 25,241,633 | 215,451,702 |
| 2021 | 50,484,003 | 45,930,472 | 41,871,031 | 51,321,850 | 25,237,120 | 214,844,476 |
| 2022 | 48,897,908 | 45,936,335 | 30,229,681 | 52,939,138 | 25,240,180 | 203,243,242 |
| 2023 | 48,892,610 | 45,928,040 | 29,601,491 | 52,947,238 | 24,555,680 | 201,925,059 |
| 2024 | 48,964,663 | 45,941,250 | 28,965,684 | 52,929,625 | 15,542,980 | 192,344,202 |
| 2025 | 90,531,155 | 45,942,750 | 28,317,072 | 11,361,738 | 7,492,935 | 183,645,650 |
| 2026 | 31,982,890 | - | 18,325,500 | - | 7,513,035 | 57,821,425 |
| 2027 | 31,997,980 | - | 17,682,500 | - | 7,535,645 | 57,216,125 |
| 2028 | 32,059,425 | - | 17,039,500 | - | 1,149,750 | 50,248,675 |
| 2029 | 28,195,275 | - | 16,396,500 | - | - | 44,591,775 |
| 2030 | 21,730,218 | - | 15,753,500 | - | - | 37,483,718 |
| 2031 | 21,773,073 | - | 15,110,500 | - | - | 36,883,573 |
| 2032 | 21,841,713 | - | 14,467,500 | - | - | 36,309,213 |
| 2033 | 21,909,885 | - | 13,824,500 | - | - | 35,734,385 |
| 2034 | - | - | 13,181,500 | - | - | 13,181,500 |
| Total[c] | $1,628,008,019 | $973,233,728 | $1,349,218,292 | $669,056,139 | $520,310,596 | $5,139,826,774 |

(a) The County's policy and practice has been to provide for payment of debt service on the Toll Road Tax Bonds from toll road revenues and certain other funds, and no tax has to date been collected to provide for such debt service.
(b) Includes the $191,765,000 Harris County Flood Control District Contract Tax Refunding Bonds, Series 2003-B and the $139,865,000 Harris County Flood Control District Contract Tax Refunding Bonds, Series 2004A, both of which are payable from contractual payments made by the County to the Flood Control District secured by the County's limited tax.
(c) Discrepancies in totals due to rounding.
(d) Reflects debt service for the entire Fiscal Year.

**Possible Forward Refunding**

The Authority is contemplating the issuance of a series of forward refunding bonds in the approximate principal amount of $28,600,000 (the "Series 2006A Bonds") for the purpose of refunding all or a portion of the Authority's outstanding Unlimited Tax Port Improvement Bonds, Series 1996 (AMT). The Authority anticipates that the Series 2006A Bonds will be delivered in July of 2006. The Series 2006A Bonds, if and when issued, will be marketed through the distribution of a separate and distinct official statement.

Delivery of the Series 2006A Bonds is contingent upon the delivery of certain certificates, reports, and legal opinions, and the satisfaction of other conditions. Events which may prevent those conditions from being satisfied include, among others, (i) changes in law affecting the Authority, the validity or tax-exempt status thereof, (ii) the filing of certain types of litigation affecting the issuance of the Series 2006A Bonds, or (iii) the occurrence and continuation of a material event of default or an event that will result in a material event under the order authorizing the Series 2006A Bonds.

**Authorized but Unissued Bonds**

On November 7, 1989, voters of the Authority authorized the issuance of $130,000,000 of debt payable from the levy of an unlimited ad valorem tax for deepening and widening the Channel (the "1989 Election"). The Authority has issued $104,300,000 in fixed rate bonds pursuant to the 1989 Election and has authorized the remaining $25,700,000 in debt to be issued in the form of commercial paper notes over the next several years. See "Commercial Paper Program" below.

On November 2, 1999, voters of the Authority authorized the issuance of $387,000,000 of debt payable from the levy of an unlimited ad valorem tax to provide funding to pay costs of acquiring, purchasing, constructing, enlarging, extending, repairing or developing facilities or aids incident to or useful or necessary in the operation or development of the Authority's ports and waterways or in aid of navigation and commerce thereon, including, without limitation, channels and turning basins, wharves, docks, warehouses, grain elevators, bunkering facilities, railroads, floating plants and facilities, lightering and towing facilities, bulk handling facilities and appurtenances thereto (including related transportation facilities and environmental enhancements) to provide economic development (the "1999 Election"). The Authority has issued $70,000,000 in fixed rate bonds pursuant to the 1999 Election and has authorized $150,000,000 in debt to be issued in the form of commercial paper notes over the next several years. It is anticipated that the Authority also will authorize the remaining $167,000,000 in authorized but unissued debt to be issued in the form of commercial paper notes. See "Commercial Paper Program" below.

**Commercial Paper Program**

The Authority has authorized the issuance of Unlimited Tax Commercial Paper Notes, Series A (the "Series A Notes") in the aggregate principal amount of $150,000,000, pursuant to the 1989 Election and the 1999 Election. The liquidity provider for the Series A Notes is Bank of America, N.A. (the "Bank") and the maturity date of the liquidity facility is August 20, 2006, unless extended by agreement of the Authority and the Bank. The Series A Note Program is administered by the County pursuant to an interlocal agreement with the Authority. As of July 31, 2005, specific projects have been approved for no more than $30,675,000 million of Series A Notes and no more than $16,507,000 million of Series A-1 Notes. The Authority expects to issue future commercial paper notes as necessary and to periodically issue fixed rate bonds to refund such notes.

*[Remainder of this page intentionally left blank.]*

**Estimated Authority and Overlapping Ad Valorem Tax Debt**

In addition to the taxing entities mentioned above, approximately 31 cities, towns and villages, 24 independent school districts, four college districts and approximately 330 utility districts are empowered to levy taxes on property within the County.

The following summary of estimated outstanding ad valorem tax debt of taxing entities in the County was compiled by the Authority's financial advisor from a variety of sources, including Texas Municipal Reports as compiled and published by the Municipal Advisory Council of Texas. The Authority believes such sources to be reliable, but the Authority takes no responsibility for the accuracy or completeness thereof. The table reflects bonds of County-wide taxing entities outstanding as of the date shown, and of other taxing entities outstanding as of various dates. Certain entities listed below may have issued substantial amounts of tax debt since the latest available data and may have capital improvement programs requiring the issuance of a substantial amount of additional tax debt.

| | Long Term Debt Outstanding (dollar amounts in thousands) | |
|---|---|---|
| County-Wide Taxing Entities[(a)]: | | |
| Harris County Flood Control District | $ 385,230 | |
| Harris County[(b)] | 1,541,347 | |
| Port of Houston Authority[(c)] | 333,645 | $ 2,260,222 |
| Cities: | | |
| Houston[(d)] | $ 2,451,200 | |
| Other cities[(e)] | 382,229 | 2,833,429 |
| Independent School Districts, Junior College Districts and the Harris County Department of Education:[(e)] | | 6,668,987 |
| Utility Districts[(e)]: | | 2,433,209 |
| Total | | $ 14,195,847 |

(a) As of June 30, 2005. Exclusive of commercial paper transactions.
(b) Excludes all outstanding Toll Road Tax Bonds which are secured by a subordinate lien on toll road net revenues and no tax has ever been required to pay such bonds.
(c) Includes the Bonds and excludes the Refunded Obligations.
(d) Includes ad valorem tax bonds of utility districts assumed by the City of Houston and certain contract tax bonds substantially equivalent to ad valorem tax bonds.
(e) Aggregate net debt as estimated by the Municipal Advisory Council of Texas as of various dates for other cities (not including the City of Houston) located within the County, 24 independent school districts and four junior college districts and approximately 330 utility districts located within the County.

**Revenue Debt of the Authority**

In addition to the unlimited tax bonds of the Authority, the Authority issues, from time to time, debt secured by certain revenues of the Authority other than taxes. A general description of the Authority's outstanding revenue debt as of December 31, 2004, is included in the Authority's financial statements attached hereto as APPENDIX A. The Authority has not issued any additional revenue debt since December 31, 2004.

## THE AUTHORITY

**General**

The Authority is a navigation district and independent political subdivision of the State of Texas, operating pursuant to Texas statute, including Chapter 117, Acts of the 55th Legislature, Regular Session, 1957, as amended, and Chapters 60, 61, and 62 of the Texas Water Code, as amended. The Authority by statute operates independently of other governmental entities, with the exception that the County, upon request of the Authority, sets the Authority's tax rate, levies the Authority's tax and issues and authorizes the Authority's general obligation bonds and commercial paper notes. The County Auditor by statute serves as the Authority's auditor, and the County Treasurer serves as the Treasurer of the Authority. Responsibility for all other activities of the Authority is exercised by a Port Commission composed of seven commissioners. Two members of the Port Commission are appointed by the County Judge and Commissioners Court; two by the Mayor and City Council of the City of Houston, Texas; one by the Mayor and City Council of the City of Pasadena, Texas; one by the Harris County Mayors and Councils Association. The Chairman of the Port Commission is jointly appointed by the governing bodies of the County and the City of Houston.

The Authority has been a deep draft port since 1914. The Houston Ship Channel (the "Channel"), the heart of the Port of Houston ("Port") complex, extends 50 miles inland and links the City of Houston with the Gulf of Mexico. The Port consists not only of the Authority's wharves, but also a large number of privately owned wharves. The Authority had 499 regular employees on December 31, 2004; and during 2004, employed 401 casual employees from various longshoremen union halls.

**Security**

The Coast Guard has implemented heightened security measures in the Channel following the terrorist attacks in New York and Washington, D.C. on September 11, 2001. The Coast Guard is responsible for the security level in the Channel and bears the costs of such security. The Authority has not incurred any significant additional expenses for security measures beyond its historical security expenses and has not experienced any significant decline in revenues since September 11. Under the guidance of the Captain of the Port, the Authority has taken certain steps and precautions to address the possibility of future terrorist attacks.

**Recent Legislation – 2005 Special Legislative Session**

The State Legislature has held two special sessions in 2005 to consider reforms to the public school financing system which could have had an effect on the State's property tax laws. To date no actions have been taken which effect the State's property tax laws. The Authority cannot predict the any future actions of the State Legislature that might affect the Authority or the results of any future special sessions, if any.

**Business of the Authority**

The Authority owns a diverse group of facilities designed for handling general cargo, containers, grain, other dry bulk materials, project and heavy-lift cargo and virtually any other kind of cargo. In addition, the Authority leases land and railroad rights-of-way to others, licenses pipeline crossings of its property, and maintains areas for depositing dredged materials.

All of these facilities are operated for hire on a first-come, first-served basis, except for parts of the Jacintoport Terminal Wharf, Bulk Materials Handling Plant, and Care Terminal Wharf, which are subject to preferential, but not exclusive, berthing arrangements; Container Terminal 6 and a portion of Terminal 5 at Barbours Cut, which is leased to Maersk-Sea-Land Service, Inc.; the automated facility at Jacintoport, which is leased to Jacintoport International, and the grain elevator at Woodhouse Terminal which is leased to Louis Dreyfus Corporation. The privately owned wharves-for-hire located at the Port compete directly with the Authority's general cargo wharves. The Authority neither regulates the tariffs charged by, nor derives any revenues from, any of the privately owned wharves, except for certain revenues from private wharves located at Bayport.

**Port Facilities of the Authority**

The Authority owns general cargo wharves at the Turning Basin Terminal in the upper Channel area. Each wharf can berth one or more ships depending on the length of the ship. These wharves have substantial dockside facilities, including enclosed short-term storage space, enclosed long-term storage space and short-term open storage space. Wharf 32, located within this terminal, was specifically designed for handling project and heavy-lift cargoes and has 18.5 acres of heavy-duty paved marshalling area.

Woodhouse Terminal, acquired in December of 1992, is located on a 100-acre tract that is a short distance downstream from the Turning Basin Terminal. The terminal includes over 230,000 square feet of warehouse space, three general cargo wharves, roll-on/roll-off ("RO/RO") ramp, wharf side rail trackage, and a modern six-million-bushel-capacity grain elevator, which is under lease to Louis Dreyfus Corporation until December 2006.

The Authority owns two wharves for handling dry bulk cargo in the mid-Channel area. Each has the capacity for berthing one ship. A bulk materials handling plant is located at this wharf. The plant also has rail car and truck loading and unloading facilities. A portion of the plant is leased to Trans-Global Solutions until June 2009 and Excalibar Minerals on a month-to-month basis.

In the same mid-Channel area, the Authority owns Jacintoport Terminal. This approximately 125 acre terminal consists of three wharves, various warehouse facilities and buildings, and has rail trackage and other improvements. Also included are refrigerated, frozen, and dry cargo facilities used for both cargo handling and storage. All three wharves and approximately 50 acres of land are subject to the provisions of the lease between the Authority and Seaboard Corporation and Jacintoport Acquisition Partnership, LP.

Care Terminal, which is a general cargo terminal with two wharves, warehouse space, rail trackage and a paved marshaling area, was purchased in 1995. Coastal Cargo of Texas operates the terminal under a ten-year lease agreement, which expires in 2012.

The Authority also owns wharves that are used for handling liquid bulk cargo. One is a barge facility and is located in the San Jacinto Bay area. The others are ship facilities and are located in the upper Channel area. Preferential, but not exclusive, berthing rights have been granted at the barge facility and two of the ship facilities.

Barbours Cut Terminal ("BCT") provides special-purpose facilities for container, LASH (Lighter Aboard-Ship), RO/RO ships, and cruise ships. This terminal is located 25 miles downstream from the Turning Basin near the point where the Channel enters Galveston Bay and is two hours sailing time from the Gulf of Mexico. BCT's six berths provide 6,000 feet of continuous quay. Numerous wharf cranes ensure efficient and reliable handling of containers and can traverse the wharves to serve ships simultaneously or singly, as required. Container yard cranes are in use in the Authority's marshalling areas behind container berths to transfer containers to and from land carriers. This facility also includes paved marshalling areas and warehouse space. The Authority has expanded the rail ramp point at BCT and completed building additional lead track from BCT to Deer Park. Building additional lead track from Deer Park to Pasadena Junction is on hold pending the resolution of certain pipeline issues. The container freight station, a railroad ramp point and a RO/RO platform can handle the loading and unloading of ships carrying cargo on wheeled vehicles. This platform can serve ships using Container Terminal 1, RO/RO cargoes and transit shed cargoes.

Terminal 7, the last terminal planned for BCT, was completed in 1999 and is being used for Cruise Ships only. The Norwegian Cruise Line (NCL) signed a new 36-month berthing agreement and began offering year round cruises in November 2003.

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 ("EECT") located at Pier 10. The Authority plans to use the terminal to alleviate congestion at the busy BCT and accommodate container ships that must be diverted when the Channel is closed due to fog or other situations. The EECT features a continuous 1,346-foot long berth dock with a water depth of 40 feet. Other features include a paved storage area, a six-lane truck interchange station and truck scale. The Authority has fully restored three of the EECT wharf cranes for loading and unloading of containers from vessels.

**Other Facilities of the Authority**

In addition to its wharves, the Authority owns numerous miles of railroad track and rights-of-way and has ample storage yard capacity for railroad cars in the Port area. These facilities are leased to the Port Terminal Railroad Association, an association of the two-trunk line railroads serving Houston and the Houston Belt & Terminal Railway Company. The Authority also owns a 315-acre industrial park immediately landward and downstream from certain general cargo wharves in the upper Channel area. The park includes undeveloped Channel frontage. Much of this property is leased or rented to various private industries that independently maintain and operate these facilities.

The Authority also owns a four-story office building located in the Turning Basin Terminal which houses the Authority's executive offices and much of the Authority's administrative staff.

The Authority's channel and turning basin at Bayport were developed in cooperation with the Humble Oil & Refining Company (the predecessor of Exxon Company U.S.A.) and its subsidiary, Exxon Land Development Inc., formerly Friendswood Development Company, and serves the industries located in the Bayport Industrial

Complex. The Authority believes that those facilities do not compete with the Authority's port facilities located at Barbours Cut and the Turning Basin.

**Summary of Current Operations**

Through the first six months of 2005, the Authority's Operating Revenues have increased 14% from Operating Revenues for the first six months of 2004. Steel imports have increased 15% during the same period. In addition to the steel increases, general cargo is up 12%. TEUs ("twenty-foot equivalent units") have increased 15%. G&A expenses are 7% lower in 2005 compared to 2004.

**Significant Activities**

Revenue tonnage (including Bayport) totaled 32.8 million tons in 2004, up 9% from 2003. This included a 21% increase in General Cargo from 2003 to 2004 along with an 11% increase in Bulk for the same period. From 2003 to 2004, container movements within the Authority exceeded 1,437,000 TEU's, which represents an 16% increase. During 2004, the Authority's operating revenues exceeded $136.8 million, an increase of 13.2% compared to 2003.

**Authority's Capital Improvement Program**

***General.*** The Authority's capital budget for 2005 is set at $344.9 million. The majority of the expenditures are projected to be primarily for Security ($5.5 million), Barbours Cut ($42.0 million), Houston Ship Channel ($10.4 million), Woodhouse Terminal ($18.3 million), Real Estate ($64.2 million) and Bayport ($149.3 million). Funds budgeted to be used for these expenditures include the proceeds from the sale of commercial paper and port improvement general obligation bonds of $223.6 million and current funds of $121.3 million.

In addition to the expenses associated with modernization and expansion at the Authority's terminals, nearly 3.8% of the proposed expenses to be incurred during 2005 are attributable to the Authority's role as local sponsor of the Channel and those expenses associated with bringing the benefits of deep-draft navigation to Harris County. These expenses are associated with capital projects, which are not terminal specific, but are investments for the public benefit. These expenses include the $10.4 million for the widening and deepening of the Channel and $2.8 million for the maintenance of the dredge disposal sites used by facilities along the 50-mile long channel for the materials resulting from the maintenance dredging needed to utilize their docks.

In November 1999, the voters of Harris County approved the issuance of $387 million in General Obligation 2006A Bonds for the start of the construction of a new container terminal known as Bayport. Bonds in the aggregate principal amount of $70 million were issued in 2001 and $30,675,000 in commercial paper has been issued since that time. See "AUTHORITY AD VALOREM TAX DEBT–Authorized But Unissued Bonds" and "–Commercial Paper Program. "

***Houston Ship Channel.*** Dredging is continuing on the Houston Ship Channel Project, which was authorized by Congress in 1996. Activity is proceeding on schedule to allow the navigation features of the project to be completed by April 2005. The status of the various dredging projects has the Entrance Channel Extension, Entrance Channel, Lower Bay (including Bird Island renamed Evia Island and Red Fish Island) and the Lower Bayou have been completed; Mid Bay (including Mid Bay Marsh, Barge Lanes and Oyster Pads), Upper Bay (including Barge Lanes), Mid Bayou (including Goat Island) and Upper Bayou are still under construction.

The total cost of the project over the 50-year life is expected to be $705.2 million, to be shared by the federal government, the Authority and other nonfederal interests. Federal funding for the project will be approved through individual appropriation bills each fiscal year. Congress appropriated $53.5 million for fiscal year 2001, $33.8 million for fiscal year 2002, $36 million for fiscal year 2003, $35.5 million for fiscal year 2004 and $22 million for fiscal year 2005. Construction funds in the amount of $23.5 million have been requested to continue construction of the project in fiscal year 2006. The Texas Delegation to Congress will work aggressively to retain this level of funding. The voters of Harris County approved the sale of $130.0 million in bonds in the November 1989 election to fund the local share of the project. As of December 31, 2004 the Port Authority has spent $109 million towards its share of the project. Even with the addition of the barge lanes and the restoration of Red Fish Island, our local share is expected to remain within the $130.0 million approved by the voters.

As part of the Houston Ship Channel project, the Port of Houston Authority will create 4,250 acres of marsh in Galveston Bay, a bird island and boater destinations. This sort of marsh project creation using dredged material is the largest of its kind and has been extremely successful to date.

***Bayport***. A new container and cruise complex is needed to accommodate the expanding needs of existing customers and growth arising from new customers. In response to this need, in May 1998, the Port Commission approved a conceptual master plan for the Bayport Terminal Complex. The facility would be built on a site at Bayport, an industrial complex in southeast Harris County. Bayport is linked by channel to the Houston Ship Channel. Because the Bayport site is only five miles from the BCT site, customers at Bayport would benefit from the competitive rail and trucking charges and affordable ancillary services that are currently available at Barbours Cut.

At completion, the container facility at the Bayport terminal will include 7,000 feet of berth, 720 acres of container yard, buildings, equipment, cranes, an intermodal rail yard holding up to 6 trains, and an industrial development area. At capacity, the facility will be able to move 2.3 million TEUs. While the primary purpose of the Bayport Terminal Complex is to provide container terminals to keep pace with the expanding growth in container traffic, the design also includes provisions for a permanent cruise terminal. The plans would allow for the building of three cruise berths and an east-end turning basin.

Construction of Phase 1A and Planning of Phase 1 at Bayport are being done concurrently. These phases would allow for the construction of 2,500 feet of wharf, a container freight station, gate(s), administration and maintenance buildings, over 100 acres of container yard and the acquisition of 6 wharf cranes and 18 rubber-tire gantry cranes. To facilitate access to the container terminal and cruise facility, dedicated entrances are planned during later phases to divert access to and from State Highway 146. These dedicated entrances will also minimize the mixing of truck traffic with automobile traffic; and, thereby, providing a safer traffic environment. Phases IA and I would allow for the annual handling of 623,000 TEUs. Phases IA and I and the first phase of the cruise terminal are currently estimated to cost $300 million.

The entire project, to be completed over an estimated 15 to 20 year period according to market demand, would cost approximately $1.2 billion in 1998 dollars. According to a report prepared by Martin Associates an estimated 29,151 jobs would be generated within Harris County during the project's construction phase. They also estimated that the entire project would provide 32,163 total jobs, contribute $1.42 billion in personal income, and generate $128.1 million in state and local taxes. They further stated that the economic impact of this terminal to the region would be an estimated $2.4 billion annually. The terminal, upon completion, would provide for the movement of 1.4 million containers annually.

With respect to the permitting of the facility, the Authority sought input during community meetings and workshops on the proposed plan. The Authority requested an Environmental Impact Statement ("EIS") so that community concerns would be thoroughly addressed. In October 1998 the Authority filed for the necessary permits and secured U.S. Army Corps of Engineers approval to conduct an EIS. Issues to be addressed during the permit process include the following: an analysis of alternative sites; environmental issues, such as air quality, wetlands, water quality, wildlife, visual impacts, and buffer zones; facility lighting and noise; and traffic and safety. In October 2001 the Authority submitted a revised permit application updating the facility layout.

The U.S. Army Corps of Engineers released the draft EIS in November 2001. It included an analysis of 78 alternative sites for the facility, as well as environmental issues such as air quality, wetlands, water quality, wildlife, visual impacts, buffer zones, facility lighting and noise, traffic and safety. The comment period on the draft EIS concluded on March 13, 2002, and the U.S. Army Corps of Engineers released the final EIS in May 2003. The record of decision was issued in December 2003 and the permit was issued January 2004.

The Authority is committed to being a good neighbor both during the building of the Bayport Terminal Complex and in the long term. The Authority's record of working through tough development issues, such as the widening and deepening project, is a good indicator of its concern for the health of Galveston Bay. This track record illustrates that the Authority strives for policies and programs that allow nature and industry to co-exist successfully. The Port Commission and staff have pledged to work cooperatively with its neighbors and environmental groups to accomplish its commercial goals and to provide resources and synergy for a beneficial and productive Galveston Bay.

### Table 7 — Table of Physical Characteristics of the Port Facilities of the Authority

| | Berth Lengths (Feet) | Water Depth Below Mean Tide (Feet) | Paving Marshalling Area (Acres) | Covered Storage (Sq. Ft.) |
|---|---|---|---|---|
| **Turning Basin Terminal** | | | | |
| 48 general cargo wharves | 376-600 | 27-37* | 27.3 | 1,400,000 |
| 5 liquid bulk wharves | 226-570 | 28-36* | -- | -- |
| Wharf — 32-heavy duty cargo | 800 | 37* | 20.2 | -- |
| **Woodhouse Terminal **** | | | | |
| Wharf 1 | 660 | 39* | 2.2 | -- |
| Wharves 2 and 3 | 1,250 | 35 | -- | 231,750 |
| Grain Dock | 600 | 40 | -- | -- |
| **Dry Bulk Cargo Facility** | | | | |
| Wharf | 800 | 42 | -- | -- |
| Lay Berth | 400 | 42 | -- | -- |
| **Jacintoport** | | | | |
| Wharves 1— 3 | 1830 | 38 | 7.5 | 82,500 |
| **Care Terminal** | | | | |
| Wharf 1 | 500 | 36 | 9.6 | 45,000 |
| Wharf 2 | 618 | 38 | 4.0 | -- |
| **San Jacinto Bay Barge Facility** | | | | |
| Barge Berth | 320 | 12 | -- | -- |
| **Upper Channel Bulk Cargo Facilities** | | | | |
| Berths | 200-700 | 26-40 | -- | -- |
| **Barbours Cut Terminal** | | | | |
| LASH Berth | 950 | 40 | -- | -- |
| Container Berths 1 — 6 | 6,000 | 40 | 230 | 255,000 |
| **Passenger Berth** | 900 | 40 | | |
| **Galveston** | | | | |
| Container Berths 1 and 2 | 1,350 | 40 | 36 | 229,860 |

* The maximum depth of the Channel in this area.

** Woodhouse Terminal is the location of Houston Public Grain Elevator No. 2, a 6,000,000-bushel capacity grain elevator having an average loading capacity of 80,000 bushels per hour.

## Equipment

**Turning Basin Terminal:** two 40 long ton capacity container cranes which serve nine berths on a rental basis. Privately-owned mobile cranes and additional cargo handling equipment are available for hire on an hourly basis.

**Barbours Cut Terminal:**

**Container Cranes:** six 40-ton and five 50-ton and Maersk-Sealand has two 30-ton.
**Container Yard Cranes:** forty-one 40-ton.
**Other Cranes:** four 30,000 pound lifters for handling empty containers and three 40 long ton container handling machines.
**Other Equipment:** 33 heavy-duty yard tractors and 125 heavy-duty yard chassis are available for rent from the Authority.

**Galveston:**

**Container Cranes:** four 40-ton
**Yard Cranes:** one 40-ton
**Other Equipment:** 31 heavy duty terminal tractors and 22 yard chassis and nine 35-long ton container handling top loaders.

*Source: Port of Houston Authority, Audited Financial Statements.*

### Financial Condition and Operations

The following summary tables of the Authority's Financial Condition and Operations for the fiscal years ended December 31, 2000 through 2004 have been prepared by the Authority.

**Table 8 — Summary of Comparative Statement of Net Assets**

(dollar amounts in thousands)

| | 2004 | 2003 | 2002 | 2001 | 2000 |
|---|---|---|---|---|---|
| Current and Other Assets | $ 402,655 | $ 416,158 | $ 422,913 | $ 415,499 | $ 332,008 |
| Capital Assets | 658,859 | 607,408 | 572,168 | 541,687 | 513,599 |
| Total Assets | $1,061,514 | $1,023,566 | $ 995,081 | $ 957,186 | $ 845,607 |
| Long-Term Liabilities | $ 327,345 | $ 344,895 | $ 376,286 | $ 372,759 | $ 284,766 |
| Other Liabilities | 43,270 | 37,027 | 23,296 | 23,436 | 47,849 |
| Total Liabilities | $ 370,615 | $ 381,922 | $ 399,582 | $ 396,195 | $ 332,615 |
| Invested in capital assets, net of related debt | $ 431,595 | $397,063 | $ 359,244 | $ 337,229 | $ 336,140 |
| Restricted | 59,403 | 57,844 | 56,928 | 53,024 | 19,015 |
| Unrestricted | 199,901 | 186,737 | 179,327 | 170,738 | 157,837 |
| Total Net Assets | $ 690,899 | $ 641,644 | $ 595,499 | $ 560,991 | $ 512,992 |
| Total Equity and Liabilities | $1,061,514 | $1,023,566 | $ 995,081 | $ 957, 186 | $ 845,607 |

*Source: Port of Houston Authority, Audited Financial Statements for the fiscal years indicated.*

**Table 9 – Survey of Comparative Historical Operations**

(dollar amounts in thousands)

| | 2004 | 2003 | 2002 | 2001 | 2000 |
|---|---|---|---|---|---|
| Operating Revenues | $136,813 | $120,902 | $108,331 | $108,339 | $108,140 |
| Operating Expenses | 121,839 | 114,010 | 106,787 | 95,518 | 85,134 |
| Operating Earnings | 14,974 | 6,892 | 1,544 | 12,821 | 23,006 |
| Non-Operating Revenues | 7,261 | 10,274 | 4,335 | 11,964 | 8,680 |
| Income before Property Tax Revenue | 22,235 | 17,166 | 5,879 | 24,785 | 31,686 |
| Non-Operating Revenues Related to Property Taxes | 24,111 | 28,109 | 28,615 | 23,214 | 22,965 |
| Contributions to/from federal or state agency | 2,909 | 870 | 14 | 0 | 4,712 |
| Net Income | $ 49,255 | $ 46,145 | $ 34,508 | $ 47,999 | $ 59,363 |

*Source: Port of Houston Authority, Audited Financial Statements for the fiscal years indicated.*

**Table 10 - Table of Annual Cargo Amounts**

In 2003 the entire Port of Houston (which includes facilities not owned by the Authority) ranked first in foreign tonnage and second in the United States in total tonnage. The following table shows the amount of cargo handled by the entire Port of Houston for each of the years 1995-2004.

(in thousands)

| Year | Short Tons |
|---|---|
| 2004 | (a) |
| 2003 | 190,923 |
| 2002 | 177,561 |
| 2001 | 185,050 |
| 2000 | 186,567 |
| 1999 | 158,828 |
| 1998 | 169,070 |
| 1997 | 165,456 |
| 1996 | 148,183 |
| 1995 | 135,231 |

(a) Amount not available until 2006.
*Source: U.S. Corps of Engineers.*

## INVESTMENTS

The Authority invests its investable funds in investments authorized by State law in accordance with written investment policies approved by the Port Commissioners of the Authority, a copy of which is available upon request. Both state law and the Authority's investment policies are subject to change.

The Office of the Controller of the Authority invests all funds of the Authority. The Department of Financial Services of the County acts as an investment agent on behalf of the Authority. The Authority and the County have separate investment portfolios that are not commingled into a single pool of investments.

**Investment Strategy and Policy**

Under State law, the Authority is required to invest its funds under a written investment strategy and policy that primarily emphasizes safety of principal and liquidity and that addresses investment diversification, yield, maturity, and the quality and capability of investment management. All Authority funds must be invested in investments that are consistent with the operating requirements of the Authority. The Authority's written investment policy specifically excludes investments in bankers' acceptances.

In practice, the Authority's investments are limited to obligations of the United States or its agencies and instrumentalities, collateralized mortgage obligations, certificates of deposit, fully collateralized repurchase agreements, commercial paper, municipal obligations rated AA or higher, and money market mutual funds. Under State law, Authority investments must be made "with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived."

Under Texas law, the Authority is authorized to invest in (1) bonds of the United States or its agencies or instrumentality's, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) collateralized mortgage bonds directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States, (4) other obligations, the principal of and interest on which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State of Texas or the United States or their respective agencies and instrumentalities, (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than "A" or its equivalent, (6) certificates of deposit that are guaranteed or insured by the Federal Deposit Insurance Corporation or are secured as to principal by obligations described in the preceding clauses or in any other manner and amount provided by law for Authority deposits, (7) certificates of deposit and share certificates issued by a state or federal credit union domiciled in the State of Texas that are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund, or are secured as to principal by obligations described in the clauses (1) through (5) or in any other manner and amount provided by law for Authority deposits, (8) fully collateralized repurchase agreements that have a defined securities dealer or a financial institution doing business in the State of Texas, (9) bankers' acceptance with a remaining term of 270 days or less, if the short-term obligations of the accepting bank or its parent are rated at least "A-1" or "P-1" or the equivalent by at least one nationally recognized credit rating agency, (10) commercial paper that is rated at least "A-1" or "P-1" or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (11) no-load money market mutual funds registered with and regulated by the Securities and Exchange Commission that provides the investing entity with a prospectus and other information required by the Securities Exchange Act of 1934 or the Investment Company Act of 1940 and that has a dollar weighted average portfolio maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of $1 for each share, and (12) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, invests exclusively in bonds described in the preceding clauses; and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than "AAA" or its equivalent, (13) obligations issued, assumed, or guaranteed by the State of Israel, and (14) guaranteed investment contracts that have a defined termination date and are secured by obligations described in clause (1) above in an amount at least equal to the amount of the bond proceeds invested under such contract.

**Current Investments**

The following percentages of the Authority's investable funds were invested in the following categories of investments as of December 31, 2004. The average remaining maturity of such investments was 183 days based on par value.

**Table 11 - Schedule of Distribution of Authority Investments**

| Distribution of Investments | |
|---|---|
| Money Market Deposits | 60 % |
| U.S. Government Agencies Securities | 34 |
| Commercial Paper | 5 |
| Municipal Bonds | 1 |
| TOTAL | 100% |

## AUTHORITY RETIREMENT PLAN

The Port of Houston Authority Restated Retirement Plan (the "Plan") is a single-employer noncontributory defined benefit plan covering all permanent, full-time employees after the completion of one year of employment. 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, 2004 and 2003 was $23,170 (84% of the total payroll of $27,661) and $21,969 (81% of total payroll of $27,106), respectively.

## GASB 45 IMPLICATIONS FOR THE AUTHORITY

In July 2004, the Governmental Accounting Standards Board issued Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions." The objective of this statement is to address how state and local governments should account for and report their costs and obligations related to post-employment healthcare and other non-pension benefits ("OPEB"). The statement generally requires that state and local governmental employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. According to the phase in criteria, this statement is effective for periods beginning after December 15, 2006. Management of the Authority has not determined the impact, if any, upon its financial position, results of operations, or cash flows upon adoption.

## REGULATION AND LITIGATION

### Environmental Regulations

***Regional Air Quality.*** Under the Clean Air Act Amendments of 1990, the eight-county Houston-Galveston Consolidated Metropolitan Statistical Area was designated by the Environmental Protection Agency ("EPA") as a severe non-attainment area under the 1-hour ozone standard. EPA required the Texas Commission on Environmental Quality ("TCEQ") to develop a State Implementation Plan ("SIP") demonstrating that the Houston-Galveston area would attain the 1-hour standard by 2007. TCEQ successfully developed this SIP. The SIP was approved by the EPA on October 15, 2001.

The 1-hour ozone SIP includes numerous volatile organic compound ("VOC") and nitrogen oxide ("NOx") emission controls designed to reduce ozone levels in the Houston-Galveston area. Compliance dates for emission controls specified in the SIP are generally set for between 2002 and 2006, depending on the rule. In 2004, the TCEQ primarily focused on evaluating whether the determined control measures would suffice or whether additional reductions would be necessary to meet the 1-hour ozone standard. This evaluation process was called the "mid-course correction" and was a commitment made by TCEQ in the 1-hour SIP. On December 1, 2004, TCEQ approved the mid-course correction, which provided rules for further emission controls and recoded rules for failure of enforceability. The TCEQ concentrated on developing rules for Highly Reactive Organic Compounds (HRVOCs) and revoked the Heavy Duty Diesel Engine Idling Rule due to lack of assigned authority for enforcement.

In addition to the emission reductions required under the 1-hour SIP, and Mid-Course Correction SIP, further emission reductions will be required to achieve EPA's new more stringent ozone standard -- the 8-hour ozone standard. EPA issued the 8-hour ozone standard in July 1997. EPA found that the 1-hour standard was inadequate for protecting public health. Scientific studies showed that ozone could affect human health at lower levels and over longer exposure times that one hour.

The 8-hour ozone standard was litigated for several years, but on April 15, 2004, EPA designated the Houston/Galveston area as a "moderate" non-attainment area under the new standard. The TCEQ now must develop an 8-hour ozone SIP by July 2007. This new SIP must demonstrate that the Houston/Galveston area will attain the 8-hour ozone standard by 2010.

***Port of Houston Authority***. The Authority has undertaken a number of environmental-related initiatives in the last several years. The Authority was selected by the EPA to participate in a local government Environmental Management System ("EMS") Initiative. An EMS is a set of management processes and procedures that allow an organization to analyze, control, and reduce the environmental impact of the organization's activities, products and services and operate with greater efficiency and control. Benefits expected include improved overall environmental performance (including areas not currently regulated), expanded pollution prevention opportunities and improved compliance. The EPA and TCEQ recognized the Authority as the first port in the United States to achieve compliance with the ISO 14001 standards for its EMS for the BCT and Central Maintenance Facilities. Additionally, the Authority continues participation in the EPA's National Environmental Performance Track program.

With respect to air quality issues, the Authority has also undertaken a number of initiatives in order to allow continued productivity at the marine terminals while still allowing the region to meet air quality goals. Such initiatives include a fuel emulsion, particulate traps and fuel vapor enhancer demonstration projects and refinements of emissions inventories. With the success of the fuel emulsion project, the Authority received grant funding through TERP to expand the program to 61 pieces of equipment. The Authority has also been successful in receiving TERP funding for the replacement of a fireboat engine and the purchase of seven new pieces of cargo handling equipment. In December 2004, the Authority was approved for an EPA Voluntary Diesel Retrofit Program grant, in the amount of $150,000, to demonstrate emission reductions from a diesel emulsion and diesel oxidation catalyst on cargo-handling equipment.

### Area Topography and Land Subsidence

The land surface in certain areas of Harris County has subsided several feet since 1943 and the subsidence is continuing. The principal causes of subsidence are considered to be the withdrawal of groundwater and, to a lesser extent, oil and gas production. Subsidence may impair development in certain areas and expose such areas to flooding and severe property damage in the event of storms and hurricanes, and thus may affect assessed valuations in those areas. In 1975 the Texas Legislature created the Harris-Galveston Coastal Subsidence District (HGCSD) to provide regulatory control over the withdrawal of groundwater in Harris and Galveston Counties in an effort to limit subsidence. This state agency, with no powers to levy taxes or incur debt, encompasses an area, which includes the existing surface water supplies, provides an alternative source of water to meet many industrial and domestic water needs and, with the reduction of withdrawal of groundwater, the rate of subsidence has been reduced. The Authority completes annual water usage reporting to the HGCSD, annual permitting and participates in the Water Wise Education Program in local schools for resource management through the HGCSD.

### Pending Litigation

The Authority is a 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.

In 1998, the Authority was sued in state court by plaintiff pipeline companies that own pipelines crossing the Houston Ship Channel at various points. The Authority subsequently removed the action to federal district court. The United States Army Corps of Engineers was also a defendant. The plaintiffs alleged that the Authority should bear the costs of removal or relocation of their pipelines in connection with widening and deepening of the Houston Ship Channel. In 2002, the federal district court entered judgment against the Authority concluding that the Authority, and not the plaintiffs, was responsible for the costs of pipeline removal and relocation. On January 30, 2004, the Fifth Circuit unanimously vacated the federal district court's order and rendered judgment in favor of the Authority and the U.S. Army Corp of Engineers. On April 1, 2004, the Fifth Circuit denied the plaintiffs' petition for rehearing, and on October 4, 2004, the United State Supreme Court denied the plaintiffs' petition for writ of certiorari, concluding the matter.

## BONDHOLDERS' REMEDIES

The Orders pursuant to which the Bonds are issued obligate the Commissioners Court to levy, assess, and collect, separate annual ad valorem taxes which will be sufficient to pay when due principal of and interest on the Bonds. The Orders, however, make no provisions for (1) other security for the payment of the Bonds, (2) express remedies in the event of default, (3) acceleration of maturity of the Bonds if default occurs, or (4) a trust to protect the rights of the owners of the Bonds.

Although a registered owner of the Bonds could presumably obtain a judgment against the Authority, if a default occurred in the payment of principal of or interest on the Bonds, such judgment could not be satisfied by execution against any property of the Authority. The only principal remedy, if a default occurs, is a mandamus proceeding to compel the Commissioners Court to levy, assess and collect a separate unlimited annual ad valorem tax sufficient to pay the principal of and interest on the Bonds as it becomes due. It might be necessary to enforce such remedy on a periodic basis, because no provision exists in the Orders or otherwise for acceleration of maturity of the Bonds.

The enforcement of a claim for payments of principal of or interest on the Bonds, including the remedy of mandamus, would be subject to the applicable provision of the federal bankruptcy laws and to any other similar laws affecting the rights of creditors of political subdivisions generally.

## TAX MATTERS

### Tax Exemption

In the opinion of Andrews Kurth LLP, Houston, Texas, Bond Counsel, (a) interest on the Bonds is excludable under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), from gross income of the owners thereof for federal income tax purposes (except with respect to interest on the Series 2005A Bonds for any period during which any Series 2005A Bond is held by a "substantial user" or a "related person" thereto as provided in Section 147(a) of the Code), (b) the Series 2005A Bonds are "private activity bonds" under the Code and therefore, interest on the Series 2005A Bonds is an item of tax preference for purposes of determining the alternative minimum tax imposed on individuals and corporations, and (c) the Series 2005B Bonds are not "private activity bonds" under the Code and, therefore, interest on the Series 2005B Bonds is not an item of tax preference for purposes of determining the alternative minimum taxable income of individuals or corporations, except as described below.

The foregoing opinions of Bond Counsel are based on the Code and the regulations, rulings and court decisions thereunder in existence on the date of issue of the Bonds. Such authorities are subject to change and any such change could prospectively or retroactively result in the inclusion of the interest on the Bonds in gross income of the owners thereof or change the treatment of such interest for purposes of computing alternative minimum taxable income.

In rendering its opinions, Bond Counsel has assumed continuing compliance by the Authority with certain covenants of the Authority Orders authorizing the issuance of the Bonds and has relied on representations by the Authority with respect to matters solely within the knowledge of the Authority, which Bond Counsel has not independently verified. The covenants and representations relate to, among other things, the use of proceeds of the Bonds and any facilities financed therewith, the source of repayment of the Bonds, the investment of proceeds of the Bonds and certain other amounts prior to expenditure, and requirements that excess arbitrage earned on the investment of proceeds of the Bonds and certain other amounts be paid periodically to the United States and that the Authority file an information report with the Internal Revenue Service. If the Authority should fail to comply with the covenants in the Authority Orders, or if its representations relating to the Bonds that are contained in the Authority Orders should be determined to be inaccurate or incomplete, interest on the Bonds could become taxable from the date of delivery of the Bonds, regardless of the date on which the event causing such taxability occurs.

The Code imposes an alternative minimum tax on the "alternative minimum taxable income" of an individual, if the amount of such alternative minimum tax is greater than the amount of such individual's regular income tax. Generally, the alterative minimum taxable income of an individual or corporation will include items of tax preference under the Code, such as the amount of interest received on private activity bonds, such as the Series 2005A Bonds, issued after August 7,1986. Accordingly, Bond Counsel's opinion will state that interest on the Series 2005A Bonds is an item of tax preference includable in alternative minimum taxable income for purposes of determining the alternative minimum tax imposed on individuals and corporations. Because interest on tax-exempt obligations, such as the Series 2005B Bonds, is included in a corporation's "adjusted current earnings," ownership of the Series 2005B Bonds could subject a corporation to alternative minimum tax consequences.

Except as stated above, Bond Counsel will express no opinion as to any federal, state or local tax consequences resulting from the ownership of, receipt or accrual of interest on or acquisition or disposition of the Bonds.

Bond Counsel's opinion is not a guarantee of a result, but represents its legal judgment based upon its review of existing statutes, regulations, published rulings and court decisions and the representations and covenants of the Authority described above. No ruling has been sought from the Internal Revenue Service (the "Service") with respect to the matters addressed in the opinion of Bond Counsel, and Bond Counsel's opinion is not binding on the Service. The Service has an ongoing program of auditing the tax-exempt status of the interest on municipal obligations. If an audit of the Bonds is commenced, under current procedures the Service is likely to treat the Authority as the "taxpayer," and the owners of the Bonds may have no right to participate in the audit process. In responding to or defending an audit of the tax-exempt status of the interest on the Bonds, the Authority may have different or conflicting interests from the owners of the Bonds. Public awareness of any future audit of the Bonds could adversely affect the value and liquidity of the Bonds during the pendency of the audit, regardless of its ultimate outcome.

Under the Code, taxpayers are required to provide information on their returns regarding the amount of tax-exempt interest, such as interest on the Bonds, received or accrued during the year.

Prospective purchasers of the Bonds should be aware that the ownership of tax-exempt obligations, such as the Bonds, may result in collateral federal income tax consequences to, among others, financial institutions, life insurance companies, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations, and individuals otherwise eligible for the earned income tax credit. Such prospective purchasers should consult their tax advisors as to the consequences of investing in the Bonds.

If a tax-exempt obligation, such as the Bonds, was acquired at a "market discount" and if the fixed maturity of such obligation is equal to, or exceeds, one year from the date of issue, the Code provides ordinary income tax treatment of gain recognized upon the disposition of such "market discount bond." A "market discount bond" is one which is acquired by the holder at a purchase price which is less than the stated redemption price at maturity or, in the case of a bond issued at an original issue discount, the "revised issue price" (*i.e.*, a market discount). Such treatment applies to "market discount bonds" to the extent the gain from the disposition thereof exceeds the accrued market discount of such bonds unless a statutory *de minimis* rule applies. The "accrued market discount" is the amount which bears the same ratio to the market discount as the number of days during which the holder holds the obligation bears to the number of days between the acquisition date and the final maturity date. The applicability of the market discount rules may adversely affect the liquidity or secondary market price of the Bonds. Purchasers should consult their own tax advisors regarding the potential implications of market discount with respect to the Bonds.

**Tax Treatment Of Original Issue Discount And Premium Bonds**

**Discount Bonds.** According to representations of the Underwriters, certain of the Bonds are being offered at initial offering prices which are less than the stated redemption prices at maturity of such Bonds. If the initial offering prices of the Bonds are lower than the stated redemption price payable at maturity, the Bonds of that maturity (the "Discount Bonds") will be considered to have "original issue discount" for federal income tax purposes. An initial owner who purchases a Discount Bond in the initial public offering of the Bonds at such an initial offering price will acquire such Discount Bond with original issue discount equal to the difference between (a) the stated redemption price payable at the maturity of such Discount Bond and (b) the initial public offering price to the public of such Discount Bond. Under existing law, such original issue discount will be treated for federal income tax purposes as additional interest on a Bond and such initial owner will be entitled to exclude from gross income for federal income tax purposes that portion of such original issue discount deemed to be earned (as discussed below) during the period while such Discount Bond continues to be owned by such initial owner. Except as otherwise provided herein, the discussion regarding interest on the Bond under the caption "Tax Exemption" generally applies to original issue discount deemed to be earned on a Discount Bond while held by an owner who has purchased such Bond at the initial offering price in the initial public offering of the Bonds and that discussion should be considered in connection with this portion of the Official Statement.

In the event of a redemption, sale, or other taxable disposition of a Discount Bond prior to its stated maturity, however, any amount realized by such initial owner in excess of the basis of such Discount Bond in the hands of such owner (increased to reflect the portion of the original issue discount deemed to have been earned while such Discount Bond continues to be held by such initial owner) will be includable in gross income for federal income tax purposes.

Because original issue discount on a Discount Bond will be treated for federal income tax purposes as interest on a Bond, such original issue discount must be taken into account for certain federal income tax purposes as it is deemed to be earned even though there will not be a corresponding cash payment. Corporations that purchase Discount Bond must take into account original issue discount as it is deemed to be earned for purposes of determining alternative minimum tax. Other owners of a Discount Bond may be required to take into account such original issue discount as it is deemed to be earned for purposes of determining certain collateral federal tax consequences of owning a Bond. See "Tax Exemption" for a discussion regarding the alternative minimum taxable income consequences for corporations and for a reference to collateral federal tax consequences for certain other owners.

The characterization of original issue discount as interest is for federal income tax purposes only and does not otherwise affect the rights or obligations of the owner of a Discount Bond or of the Authority. The portion of the principal of a Discount Bond representing original issue discount is payable upon the maturity or earlier redemption of such Bond to the registered owner of the Discount Bond at that time.

Under special tax accounting rules prescribed by existing law, a portion of the original issue discount on each Discount Bond is deemed to be earned each day. The portion of the original issue discount deemed to be earned each day is determined under an actuarial method of accrual, using the yield to maturity as the constant interest rate and semi-annual compounding.

The federal income tax consequences of the purchase, ownership, redemption, sale or other disposition of Discount Bonds by an owner that did not purchase such Bonds in the initial public offering and at the initial offering price may be determined according to rules which differ from those described above. All prospective purchasers of Discount Bonds should consult their tax advisors with respect to the determination for federal, state and local income tax purposes of interest and original issue discount accrued upon redemption, sale or other disposition of such Discount Bonds and with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of such Discount Bonds.

**Premium Bonds.** According to representations of the Underwriters, certain of the Bonds are being offered at initial offering prices which exceed the stated redemption prices payable at the maturity of such Bonds. If any of the Bonds of such maturities are sold to members of the public (which for this purpose excludes bond houses, brokers and similar person or organizations acting in the capacity of wholesalers or underwriters) at such initial offering prices, each of the Bonds of such maturities ("Premium Bonds") will be considered for federal income tax purposes to have "bond premium" equal to the amount of such excess. The basis for federal income tax purposes of a Premium Bond in the hands of an initial purchaser who purchases such Bond in the initial offering must be reduced each year and upon the sale or other taxable disposition of the Bond by the amount of amortizable bond premium. This reduction in basis will increase the amount of any gain (or decrease the amount of any loss) recognized for federal income tax purposes upon the sale or other taxable disposition of a Premium Bond by the initial purchaser. Generally, no corresponding deduction is allowed for federal income tax purposes, for the reduction in basis resulting from amortizable bond premium. The amount of bond premium on a Premium Bond which is amortizable each year (or shorter period in the event of a sale or disposition of a Premium Bond) is determined under special tax accounting rules which use a constant yield throughout the term of the Premium Bond based on the initial purchaser's original basis in such Bond .

THE FEDERAL INCOME TAX CONSEQUENCES OF THE PURCHASE, OWNERSHIP, REDEMPTION, SALE OR OTHER DISPOSITION BY AN OWNER OF BONDS THAT ARE NOT PURCHASED IN THE INITIAL OFFERING OR WHICH ARE PURCHASES AT AN AMOUNT REPRESENTING A PRICE OTHER THAN THE INITIAL OFFERING PRICES FOR THE BONDS OF THE SAME MATURITY MAY BE DETERMINED ACCORDING TO RULES WHICH DIFFER FROM THOSE DESCRIBED ABOVE. MOREOVER, ALL PROSPECTIVE PURCHASERS OF BONDS SHOULD CONSULT THEIR TAX ADVISORS WITH RESPECT TO THE FEDERAL, STATE, LOCAL AND FOREIGN TAX CONSEQUENCES OF THE PURCHASE, OWNERSHIP, REDEMPTION, SALE OR OTHER DISPOSITION OF PREMIUM BONDS.

## LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

Section 1201.041 of the Public Securities Procedures Act (Chapter 1201, Texas Government Code, as amended) provides that the Bonds are negotiable instruments; are investment securities governed by Chapter 8, Texas Business and Commerce Code; and are legal and authorized investments for insurance companies, fiduciaries, and trustees, and for the sinking fund of municipalities or other political subdivisions or public agencies of the State of Texas. The Bonds are eligible to secure deposits of any public funds of the state, its agencies and political subdivisions, and are legal security for those deposits to the extent of their market value. For political subdivisions in the State which have adopted investment policies and guidelines in accordance with the Public Funds Investment Act (V.T.C.A., Government Code, Chapter 2256), the Bonds may have to be assigned a rating of "A" or its equivalent as to investment quality by a national rating agency before such obligations are eligible investments for sinking funds and other public funds. No review by the Authority has been made of the laws in other states to determine whether the Bonds are legal investments for various institutions in those states.

The Authority has made no investigation of any other laws, rules, regulations, or investment criteria that might affect the suitability of the Bonds for any of the above-purposes or limit the authority of any of the above persons or entities to purchase or invest in the Bonds.

## LEGAL MATTERS

The delivery of the Bonds is subject to the approving opinions of the Attorney General of Texas and the legal opinions of Andrews Kurth LLP, Houston, Texas, Bond Counsel, as to the validity of the Bonds under the Constitution and laws of the State of Texas. The opinions of Bond Counsel will be based upon an examination of transcripts of certain proceedings taken by the Authority incident to the issuance and delivery of the Bonds. Certain legal matters will be passed upon for the Underwriters by Winstead Sechrest & Minick P.C., Houston, Texas, Underwriters' Counsel.

The fees of Bond Counsel and Underwriters' Counsel for their services with respect to the Bonds are contingent upon the issuance and delivery of the Bonds.

## CONTINUING DISCLOSURE OF INFORMATION

In the Authority Orders, the Authority made the following agreement for the benefit of the holders and beneficial owners of the Bonds. The Authority is required to observe this agreement for so long as it remains obligated to advance funds to pay the Bonds. Under the Authority Orders, the Authority will be obligated to provide certain updated financial information and operating data annually and timely notice of specified material events, to certain information vendors. This information is available to securities brokers and others who subscribe to receive information from the vendors.

### Annual Reports

The Authority annually will provide certain updated financial information and operating data to all NRMSIRs and any SID, defined below. The information to be updated includes all quantitative financial information and operating data of the general type included in this Official Statement in APPENDIX A and under schedules listed in APPENDIX C. The Authority will update and provide this information within six months after the end of each fiscal year. The Authority will provide updated information to each nationally recognized municipal securities information repository ("NRMSIR") and any state information depository ("SID") designated for the State and approved by the staff of the United States Securities and Exchange Commission (the "SEC").

The Authority may provide updated information in full text, or may incorporate by reference other publicly available documents, or in such other form consistent with the agreement, as permitted by SEC Rule 15c2-12 (the "Rule"). The updated information will include audited financial statements if the Authority commissions an audit and the audit is completed by the required time. If audited financial statements are not available by the required time, the Authority will provide audited financial statements when and if they become available, but if such audited financial statements are unavailable, the Authority will provide such financial statements on an unaudited basis and any additional financial information required within this Official Statement within the required time. Any such financial statements will be prepared in accordance with the accounting principles described in APPENDIX A or such other accounting principles as the Authority may be required to employ from time to time pursuant to State law or regulation.

The Authority's current fiscal year-end is the last day of December. Accordingly, the Authority must provide updated information by June 30 in each year, unless the Authority changes its fiscal year. If the Authority changes its fiscal year, it will notify each NRMSIR and any SID of the change.

### Secondary Market Disclosure

The Municipal Advisory Council of Texas has received Securities and Exchange Commission approval to operate, and has begun to operate, a "central post office" for secondary market disclosure filings made by issuers of municipal obligations such as the Authority. An issuer may submit its secondary market disclosure filings to the central post office, which will then transmit the filings to the NRMSIRs, the MSRB, and the appropriate SID for filing, where applicable. This central post office can be accessed and utilized by issuers at www.DisclosureUSA.com ("DisclosureUSA"). The Authority intends to utilize DisclosureUSA for the filing of secondary market disclosure filings relating to the Bonds, but may discontinue making such filings through DisclosureUSA and utilize any other method of filing permitted by federal securities law at any time.

### Material Event Notices

The Authority also will provide timely notices of certain events to certain information vendors. Specifically, the Authority will provide notice of any of the following events with respect to the Bonds, if such event is material to a decision to purchase or sell Bonds: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the tax-exempt status of the Bonds; (7) modifications to rights of holders of the Bonds; (8) bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds; and (11) rating changes. Neither the Bonds, the Orders, nor the Authority Orders make any provision for credit or liquidity enhancement or requiring the funding of debt service reserves. In addition, the Authority will provide timely notice of any failure by the Authority to provide annual financial information or operating data and audited financial statements in accordance with its agreement described above under "Annual Reports." The Authority will provide each notice described in this paragraph to any SID and to either each NRMSIR or the Municipal Securities Rulemaking Board (the "MSRB").

### Availability of Information from NRMSIRs and SID

The Authority has agreed to provide the foregoing information only to NRMSIRs and any SID. The information will be available to holders of and beneficial owners of the Bonds only if the holders comply with the procedures and pay the charges established by such NRMSIRs or SID or obtain the information through securities brokers who have done so.

The Municipal Advisory Council of Texas has been designated by the State as a SID and the SEC has determined that it is a qualified SID. The address of the Municipal Advisory Council is 600 West 8th Street, P.O. Box 2177, Austin, Texas 78768-2177, and its telephone number is (512) 476-6947.

### Limitations and Amendments

The Authority has agreed to update information and to provide notices of material events only as described above. The Authority has not agreed to provide other information that may be relevant or material to a complete presentation of its financial results of operations, condition, or prospects or agreed to update any information that has been provided except as described above. The Authority makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell Bonds at any future date. The Authority disclaims any contractual or tort liability for damages resulting in whole or in part from any breach of its continuing disclosure agreement or from any statement made pursuant to its agreement, although holders of Bonds may seek a writ of mandamus to compel the Authority to comply with its agreement. Nothing in this paragraph is intended or shall act to disclaim, waive or limit the Authority's duties under federal or state securities laws.

The Authority may amend a continuing disclosure agreement to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the Authority, if the agreement, as amended, would have permitted an underwriter to purchase or sell Bonds in the offering described herein in compliance with the Rule and either the holders of a majority in aggregate principal amount of the outstanding Bonds of a series consent or any qualified person unaffiliated with the Authority (such as nationally recognized bond counsel) determines that the amendment will not materially impair the interests of the beneficial owners of the Bonds of such series. The Authority may also amend or repeal an agreement if the SEC amends or repeals the applicable provisions of the Rule or a court of final jurisdiction determines that such provisions are invalid, and the Authority may amend an agreement in its discretion in any other circumstance or manner, but in either case only to the extent that its right to do so would not prevent the representative of the Underwriters of the Bonds of such series from the Authority from purchasing such Bonds in the offering described herein in compliance with the Rule. If the Authority amends an agreement, it must include with the next financial information and operating data provided in accordance with its agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of information and operating data so provided. See "APPENDIX C—Summary of Tables and Schedules Related to Continuing Disclosure of Information."

**Compliance with Prior Undertakings**

The Authority initially became obligated to make annual disclosure of certain financial information by filing with the state information depository ("SID") and each nationally recognized municipal securities information repository ("NRMSIR") in an offering that took place in 1995. Due to an administrative oversight, certain required financial information and audited financial statements for fiscal year end 2001 were not timely filed with the SID. Certain required financial information and audited financial statements were not timely filed with the NRMSIRs for fiscal years ending 1999 through 2002. The Authority mistakenly stated it had fully complied with all aspects of Rule 15c2-12 in its Official Statements for its 2000 and 2001 bond offerings, and only disclosed the late filing to the SID in its 2002 bond offering. All financial information has since been filed, as well as a notice of late filing. The Authority has implemented procedures to ensure timely filing of all future information.

**Audited Financial Report of the Authority**

The Authority requires that an annual audit be performed by an independent public accounting firm in accordance with generally accepted auditing standards. The audit of the fiscal year ended December 31, 2004, and additional financial information are available for public inspection, or copies may be obtained by written request, to the extent permitted by law, addressed to the Controller of the Authority.

## NO-LITIGATION CERTIFICATE REGARDING BONDS

The Authority will deliver a no-litigation certificate signed by the Chairman of the Port Commission dated as of the date of, and as a condition to, delivery of the Bonds. The certificate will state that no litigation of any kind has been filed or is then pending which would restrain or enjoin the issuance or delivery of the Bonds, or which would affect the provisions made for payment of the principal of and interest on the Bonds or in any manner question the validity of the Bonds.

## FINANCIAL STATEMENTS

APPENDIX A to this Official Statement contains the financial statements of the Authority for the fiscal year ended December 31, 2004. These financial statements of the Authority as of December 31, 2004, included in this Official Statement have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report included with such financial statements in APPENDIX A. The Authority has not requested Deloitte & Touche LLP to reissue its audited financial statements and Deloitte & Touche LLP has not performed any procedures in connection with this Official Statement.

## REGISTRATION, SALE AND DISTRIBUTION

The Bonds have not been registered under the federal Securities Act of 1933, as amended (in reliance upon an exemption therefrom), or the blue sky laws of any jurisdiction. The Resolution has not been qualified under the federal Trust Indenture Act of 1939, as amended (in reliance upon an exemption therefrom).

## BOND INSURANCE

Concurrently with the issuance of the Bonds, MBIA Insurance Corporation ("MBIA") will issue its Municipal Bond Insurance Policy for the Bonds (the "Policy"). The Policy guarantees the scheduled payment of principal of and interest on the Bonds when due as set forth in the form of the Policy included as an exhibit to this Official Statement.

**The MBIA Insurance Corporation Insurance Policy**

The following information has been furnished by MBIA Insurance Corporation ("MBIA") for use in this Official Statement. Reference is made to Appendix F for a specimen of the Policy.

MBIA does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding the Policy and MBIA set forth under the heading "BOND INSURANCE". Additionally, MBIA makes no representation regarding the Bonds or the advisability of investing in the Bonds.

The MBIA Policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the Authority to the Paying Agent or its successor of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Bonds as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the MBIA Policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration, unless MBIA elects in its sole discretion, to pay in whole or in part any principal due by reason of such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any Owner of the Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such Owner within the meaning of any applicable bankruptcy law (a "Preference").

MBIA's Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Bonds. MBIA's Policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be made on an accelerated basis; (iii) payments of the purchase price of Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. MBIA's Policy also does not insure against nonpayment of principal of or interest on the Bonds resulting from the insolvency, negligence or any other act or omission of the Paying Agent or any other paying agent for the Bonds.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by MBIA from the Paying Agent or any owner of a Bond the payment of an insured amount for which is then due, that such required payment has not been made, MBIA on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such Bonds or presentment of such other proof of ownership of the Bonds, together with any appropriate instruments of assignment to evidence the assignment of the insured amounts due on the Bonds as are paid by MBIA, and appropriate instruments to effect the appointment of MBIA as agent for such owners of the Bonds in any legal proceeding related to payment of insured amounts on the Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Paying Agent payment of the insured amounts due on such Bonds, less any amount held by the Paying Agent for the payment of such insured amounts and legally available therefor.

**MBIA Insurance Corporation**

MBIA Insurance Corporation ("MBIA") is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the "Company"). The Company is not obligated to pay the debts of or claims against MBIA. MBIA is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. MBIA has three branches, one in the Republic of France, one in the Republic of Singapore, and one in the Kingdom of Spain.

The principal executive offices of MBIA are located at 113 King Street, Armonk, New York 10504 and the main telephone number at that address is (914) 273-4545.

**Regulation**

As a financial guaranty insurance company licensed to do business in the State of New York, MBIA is subject to the New York Insurance Law which, among other things, prescribes minimum capital requirements and contingency reserves against liabilities for MBIA, limits the classes and concentrations of investments that are made by MBIA and requires the approval of policy rates and forms that are employed by MBIA. State law also regulates the amount of both the aggregate and individual risks that may be insured by MBIA, the payment of dividends by MBIA, changes in control with respect to MBIA and transactions among MBIA and its affiliates.

The Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

**Financial Strength Ratings of MBIA**

Moody's Investors Service, Inc. rates the financial strength of MBIA "Aaa."

Standard & Poor's, a division of The McGraw-Hill Companies, Inc. rates the financial strength of MBIA "AAA."

Fitch Ratings rates the financial strength of MBIA "AAA."

Each rating of MBIA should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of MBIA and its ability to pay claims on its policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Bonds. MBIA does not guaranty the market price of the Bonds nor does it guaranty that the ratings on the Bonds will not be revised or withdrawn.

**MBIA Financial Information**

As of December 31, 2004, MBIA had admitted assets of $10.4 billion (unaudited), total liabilities of $7.0 billion (unaudited), and total capital and surplus of $3.4 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of June 30, 2005 MBIA had admitted assets of $10.7 billion (unaudited), total liabilities of $7.0 billion (unaudited), and total capital and surplus of $3.7 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

For further information concerning MBIA, see the consolidated financial statements of MBIA and its subsidiaries as of December 31, 2004 and December 31, 2003 and for each of the three years in the period ended December 31, 2004, prepared in accordance with generally accepted accounting principles, included in the Annual Report on Form 10-K of the Company for the year ended December 31, 2004 and the consolidated financial statements of MBIA and its subsidiaries as of June 30, 2005 and for the six month periods ended June 30, 2005 and June 30, 2004 included in the Quarterly Report on Form 10-Q of the Company for the period ended June 30, 2005, which are hereby incorporated by reference into this Official Statement and shall be deemed to be a part hereof.

Copies of the statutory financial statements filed by MBIA with the State of New York Insurance Department are available over the Internet at the Company's web site at http://www.mbia.com and at no cost, upon request to MBIA at its principal executive offices.

**Incorporation of Certain Documents by Reference**

The following documents filed by the Company with the Securities and Exchange Commission (the "SEC") are incorporated by reference into this Official Statement:

(1) The Company's Annual Report on Form 10-K for the year ended December 31, 2004; and
(2) The Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2005.

Any documents, including any financial statements of MBIA and its subsidiaries that are included therein or attached as exhibits thereto, filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of the Company's most recent Quarterly Report on Form 10-Q or Annual Report on Form 10-K, and prior to the termination of the offering of the Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof from the respective dates of filing such documents. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the Company's SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2004, and (2) the Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 2005 and June 30, 2005) are available (i) over the Internet at the SEC's web site at http://www.sec.gov; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at http://www.mbia.com; and (iv) at no cost, upon request to MBIA at its principal executive offices.

**DISCLOSURE OF GUARANTY FUND NONPARTICIPATION**: In the event the Insurer is unable to fulfill its contractual obligation under this policy or contract or application or certificate or evidence of coverage, the policyholder or certificateholder is not protected by an insurance guaranty fund or other solvency protection arrangement.

## UNDERWRITING

Lehman Brothers, as representative of the Underwriters named on the cover page, has agreed, subject to certain conditions, to purchase the Bonds from the Authority at a price of $104,218,691.23, which reflects the par amount of such Bonds, plus a premium of $6,041,377.10, less an original issue discount of $417,206.40, and less an underwriting discount of $555,479.47.

The Underwriters' obligation is subject to certain conditions precedent and they will be obligated to purchase all of the Bonds if any Bonds are purchased. The prices and other terms respecting the offering and sale of the Bonds may be changed from time to time by the Underwriters after such Bonds are released for sale, and the Bonds may be offered and sold at prices other than the initial offering prices, including sales to dealers who may sell the Bonds into investment accounts.

## RATINGS

Fitch, Inc. ("Fitch") and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P") are expected to assign their municipal bond ratings of "AAA" and "AAA" respectively, to the Bonds, based on final delivery of the Policy on the date of delivery of the Bonds.

Ratings reflect only the views of the rating companies at the time each rating is assigned, and an explanation of the significance of such ratings may be obtained from such rating agencies. There is no assurance that the ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by one or more of the rating companies, if in the sole judgment of such rating company, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Bonds. The Authority will undertake no responsibility to notify Bondholders of any such revision or withdrawal of ratings, however, the Authority must comply with the continuing disclosure requirements related to rating changes (see "CONTINUING DISCLOSURE OF INFORMATION-Material Event Notices").

## VERIFICATION OF ARITHMETICAL AND MATHEMATICAL CALCULATIONS

The issuance of the Bonds will be subject to delivery by Grant Thornton LLP, Minneapolis, Minnesota, certified public accounts (the "Accountants"), of a report of the mathematical accuracy of certain computations. The Accountants will verify from the information provided to them the mathematical accuracy as of the date of the closing on the Bonds of (1) the computations contained in the provided schedules to determine that the anticipated receipts from the Government Securities and cash deposits listed in the schedules provided by First Southwest Company, to be held in the Escrow Fund, will be sufficient to pay, when due, the principal and interest requirements of the Refunded Bonds, and (2) the computations of yield on both the Government Securities and the Bonds contained in the provided schedules used by Bond Counsel in its determination that the interest on the Bonds is excludable from the gross income of the holders thereof. The Accountants will express no opinion on the assumptions provided to them, nor as to the exemption from taxation of the interest on the Bonds. Such verification of accuracy of such mathematical computation will be based upon information and assumptions supplied by the Authority and First Southwest Company, and such verification, information and assumptions will be relied on by Bond Counsel in rendering its opinion described herein.

## FINANCIAL ADVISOR

In connection with the issuance of the Bonds, First Southwest Company (the "Financial Advisor") has assisted the Authority in the preparation of Bond-related documents. The Financial Advisor's fee for services rendered with respect to the sale of the Bonds is contingent upon the issuance and delivery of the Bonds. An affiliate of the Financial Advisor, First Southwest Asset Management, Inc. ("FSAM"), has been engaged to provide investment advisory services to the Authority, which may include the investment of bond proceeds associated with these Bonds. All fees and other remuneration received by FSAM for the provision of investment advisory services to the Authority are separate and distinct from the fees associated with this Bond issue and are not contingent upon the sale and issuance of the Bonds.

Although the Financial Advisor has read and participated in the preparation of this Official Statement, it has not independently verified any of the information set forth herein. The information contained in this Official Statement has been obtained primarily from the Authority's records and from other sources that are believed to be reliable, including financial records of the Authority, reports of consultants and other entities that may be subject to interpretation. No guarantee is made as to the accuracy or completeness of any such information. No person, therefore, is entitled to rely upon the participation of the Financial Advisor as an implicit or explicit expression of opinion as to the completeness and accuracy of the information contained in this Official Statement.

## MISCELLANEOUS

All information contained in this Official Statement is subject in all respects to the complete information contained in the original sources thereof. No opinions, estimates or assumptions whether or not expressly identified as such, should be considered statements of fact. Statements made herein regarding the Bonds are qualified in their entirety by reference to the forms thereof included in the Orders and the information with respect thereto included in the Orders.

This Official Statement was approved by the Port Commission.

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# APPENDIX A

# FINANCIAL STATEMENTS OF THE AUTHORITY

Deloitte.

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USA

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## INDEPENDENT AUDITORS' REPORT

Port Commission
Port of Houston Authority of
Harris County, Texas

We have audited the accompanying statements of net assets of the Port of Houston Authority of Harris County, Texas (the "Authority"), as of December 31, 2004 and 2003, and the related statements of revenues, expenses, and changes in net assets and of cash flows for the years then ended, which collectively comprise the Authority's basic financial statements. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Authority as of December 31, 2004 and 2003, and the respective changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and schedule of funding progress – Port of Houston Authority Restated Retirement Plan are not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Authority's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Our audit was conducted for the purpose of forming an opinion on the Authority's basic financial statements. The introductory section, statistical section and other information are presented for purposes of additional analysis and is not a required part of the basic financial statements. This supplementary information is the responsibility of the Authority's management. Such information



Member of
Deloitte Touche Tohmatsu

have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 22, 2005, on our consideration of internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte & Touche LLP

June 22, 2005

## Management's Discussion and Analysis
(unaudited)

As management of the Port of Houston Authority of Harris County, Texas ("Authority") we offer readers of the Authority's basic financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal years ended December 31, 2004, December 31, 2003 and December 31, 2002. We encourage readers to consider the information that we have furnished in our letter of transmittal, which can be found on pages 5 through 14 of this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

### Financial Highlights

- The net assets of the Authority at December 31, 2004 were $690,899. Of this amount, $199,901 are considered unrestricted net assets.
- The Authority's net assets increased by $49,255 for the fiscal year ended December 31, 2004.
- The Authority's total assets increased by $37,948 during the fiscal year ended December 31, 2004. The major component in this increase was the increase in capital assets of $51,451 offset by a decrease in restricted assets of $31,330.
- The Authority's total liabilities decreased by $11,307 during the fiscal year ended December 31, 2004 The major component in this decrease was the reduction of $22,847 in long-term debt, net of current maturities due to the debt service payments on the general obligation bonds in 2004 with no new general obligation bonds being issued in 2004.
- The Authority follows enterprise fund accounting and reporting requirements, including the accrual basis of accounting and application of all Governmental Accounting Standards Board ("GASB") pronouncements.

### Overview of Financial Statements

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements comprise the following: 1) statements of net assets, 2) statements of revenues, expenses, and changes in net assets, 3) statements of cash flows, and 4) notes to the financial statements. The basic financial statements can be found on pages 28 through 55 of this report. This report also contains other supplementary information in addition to the basic financial statements themselves.

The statements of net assets present information of all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The statements of revenues, expenses, and changes in net assets present information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected property taxes and earned but unused vacation leave).

The basic financial statements include not only the Port of Houston Authority (known as the primary government), but also two legally separate blended component units, Port Development Corporation ("PDC") and Port of Houston Authority International Corporation ("POHAIC"). Financial information for these component units is reported in conjunction with the primary government.

Since the Authority follows enterprise fund accounting and reporting requirements there are statements of cash flows included as part of the basic financial statements.

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the Authority's progress in funding its obligation to provide pension benefits to its employees and can be found on page 56 of this report.

Statistical information presented on a multi-year basis and other information including disclosures for compliance with the Securities and Exchange Commission Rule 15c2-12 are presented for the purpose of additional analysis and are not a required part of the basic financial statements. Statistical and other information can be found on pages 57 through 81 of this report.

**Financial Analysis**

By far the largest portion of the Authority's net assets (62%) reflects its investment in capital assets (e.g., land, buildings, machinery and equipment), less any related debt, used to acquire those assets, and excluding any remaining debt proceeds that are still outstanding. The Authority uses these assets to provide services to its customers; consequently these assets are not available for future spending. Although the Authority's investment in capital assets is reported net of related debt, it should be noted that the resources to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Authority's net assets (9%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets (29%) may be used to meet the Authority's ongoing obligations to employees and creditors.

**Port of Houston Authority Net Assets**

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Current and other assets | **$ 402,655** | $ 416,158 | $422,913 |
| Capital assets | **658,859** | 607,408 | 572,168 |
| Total assets | **1,061,514** | 1,023,566 | 995,081 |
| Long-term liabilities | **327,345** | 344,895 | 376,286 |
| Other liabilities | **43,270** | 37,027 | 23,296 |
| Total liabilities | **370,615** | 381,922 | 399,582 |
| Invested in capital assets, net of related debt | **431,595** | 397,063 | 359,244 |
| Restricted net assets | **59,403** | 57,844 | 56,928 |
| Unrestricted net assets | **199,901** | 186,737 | 179,327 |
| Total net assets | **$ 690,899** | $ 641,644 | $595,499 |

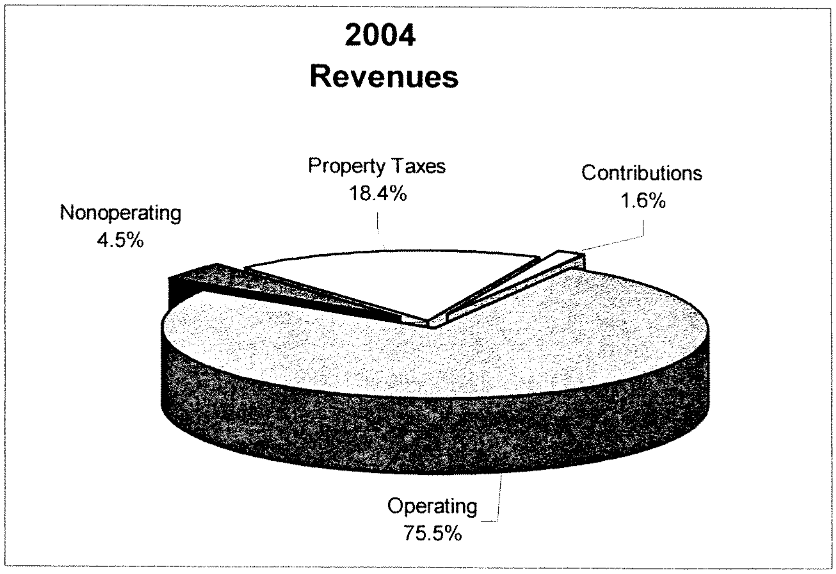
The Authority's net assets increased by $49,255 during the fiscal year ended December 31, 2004. During fiscal year 2004, net assets invested in capital net of related debt increased $34,532 with an increase in capital assets of $51,451 plus a reduction in outstanding debt net of unspent proceeds of $16,919. During fiscal year 2004, net assets restricted remained steady with a slight increase of $1,559. The remainder of the increase in net assets of $13,164 is unrestricted.

Key elements of this increase are identified in the following schedule of Changes in Net Assets and related explanations.

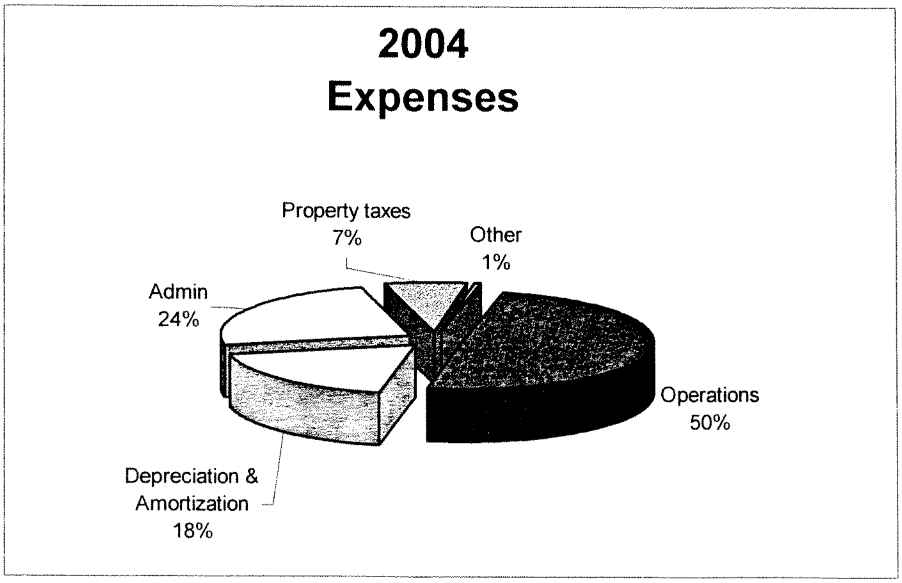
## Port of Houston Authority
## Changes in Net Assets

| | 2004 | 2003 | 2002 |
|---|---|---|---|
| **Operating revenues:** | | | |
| Vessel and cargo services | $ 116,506 | $ 101,085 | $ 88,923 |
| Rental of equipment & facilities | 15,878 | 14,977 | 15,340 |
| Grain elevator | 835 | 840 | 838 |
| Bulk materials | 2,348 | 2,978 | 2,662 |
| Other | 1,246 | 1,022 | 568 |
| **Nonoperating revenues:** | | | |
| Interest income | 2,963 | 3,243 | 5,650 |
| Other | 5,106 | 8,207 | 226 |
| **Nonoperating revenues related to property taxes:** | | | |
| Property taxes | 33,088 | 37,396 | 35,447 |
| Interest income on unlimited tax bonds | 346 | (286) | 2,179 |
| **Total Revenues** | 178,316 | 169,462 | 151,833 |
| **Operating expenses:** | | | |
| Maintenance and operation of facilities | 65,535 | 63,735 | 55,713 |
| General and administrative | 31,856 | 26,776 | 28,494 |
| Depreciation and amortization | 24,448 | 23,499 | 22,580 |
| **Nonoperating expenses-** | | | |
| Interest expense on revenue bonds | 808 | 1,176 | 1,541 |
| **Nonoperating expenses related to property taxes:** | | | |
| Interest expense on unlimited tax bonds | 8,217 | 7,639 | 7,344 |
| Property tax expense | 715 | 931 | 1,329 |
| Other, net | 391 | 431 | 338 |
| **Total Expenses** | 131,970 | 124,187 | 117,339 |
| **Income before contributions** | 46,346 | 45,275 | 34,494 |
| **Contribution from federal and state agency** | 2,909 | 870 | 14 |
| **Net Income** | 49,255 | 46,145 | 34,508 |
| **Net assets, January 1** | 641,644 | 595,499 | 560,991 |
| **Net assets, December 31** | $690,899 | $641,644 | $595,499 |

Vessel and cargo services revenues increased 15% in 2004 to $116,506. Tariffs were increased in 2004 over 2003 an average of 3%. However, tariffs for steel remained at $1.65 per short ton, which was the same as the tariff in 2003. The increase by the federal government on the tariffs on steel products enacted in 2002 was eliminated in late 2003. The decrease in bulk materials (21%) and also grain (22%) was offset by increases in bagged goods exports (25%), steel (86%), containers TEU's (16%), auto exports (28%), and general cargo (26%). Total Authority tonnage of 32.8 million tons was up 9% from 2003. Nonoperating revenues interest income in 2004 decreased $0.3 million due to market conditions, reduced investment balances and to adjust investments to market value at year end. Nonoperating revenues other decreased approximately $3 million due to the settlement of a lawsuit in 2003 in which the Authority was the plaintiff. Nonoperating revenues related to property taxes in 2004 decreased approximately $4.3 million. This was due primarily to a decrease in property taxes collected related to a decrease in the property tax rate in 2004.




Maintenance and operation of facilities expenses increased by $1.8 million (3%) from 2003. The majority of the increase was made up of the following: a) increases in salaries and benefits of $1.6 million; and b) increase in maintenance of buildings, machinery and equipment, materials and supplies of $0.2 million. General and administration expenses increased $5.1 million with the majority of the increase due to an increase in a) legal expenses of $2.7 million; b) an increase in salaries and benefits of $1.6 million and other general and administrative $.8 million. Depreciation and amortization increased $1.0 million.




**Capital Asset and Debt Administration**

**Capital assets:** The Authority's investment in capital assets as of December 31, 2004, amounts to $658.9 million (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements other than buildings, railroads, machinery and equipment, and construction-in-progress. The total increase in the Authority's investment in capital assets for the current fiscal year was 8%.

Major capital asset events during the current fiscal year included the following:

- Machinery & equipment additions totaled approximately $11.1 million in 2004 of which $7.6 million was due to the purchase of 5 RTG cranes and $1.4 million for a Navis operating system.
- Improvement other than buildings increased $14.3 million primarily due to pavement for Terminal 6 at BCT and Wharves 47 and 48 in 2004.
- Capitalized interest (net of capitalized income) totaling $6.8 million was added to the cost of assets for 2004.
- Construction-in-progress decreased $18.0 million in 2004 due primarily to the completion of various projects of the Widening and Deepening of the Houston Ship Channel which was transferred to Channel Site Land Improvements in 2004.
- Accumulated depreciation increased $21.5 million in 2004.

**PORT OF HOUSTON AUTHORITY Capital Assets**
(net of depreciation)

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| Land | **233,938** | 168,167 | $167,531 |
| Buildings | **15,453** | 17,351 | 18,492 |
| Improvements other than buildings | **190,665** | 188,528 | 177,275 |
| Railroads | **33,512** | 33,617 | 34,731 |
| Machinery and equipment | **60,794** | 57,275 | 47,936 |
| Construction-in-progress | **124,497** | 142,470 | 126,203 |
| | **$658,859** | $607,408 | $572,168 |

Additional information on the Authority's capital assets can be found in Note 5 on pages 40 and 41 of this report.

**Long-term debt:** At the end of the current fiscal year, the Authority had total long-term debt outstanding of $308.0 million (net of unamortized premium/(discount). Of this amount, $292.5 million was Unlimited Tax Port Improvement Bonds and Unlimited Tax Refunding Bonds (referred to as General Obligation Bonds) and whose debt service is paid from ad valorem taxes levied and collected by Harris County Tax Assessor and Collector. Revenue bonds of $8.7 million secured solely by the revenues of the Authority and $6.8 of Commercial Paper represents the balance of the long term debt.

Outstanding Debt
General Obligation, Revenue Bonds and Commercial Paper
(net of unamortized premium/(discount))

| | **2004** | 2003 | 2002 |
|---|---|---|---|
| General Obligation Bonds: | | | |
| Unlimited Tax Port Improvement Bonds | **$ 250.3** | $ 272.0 | $291.6 |
| Unlimited Tax Refunding Bonds | **42.2** | 38.4 | 44.2 |
| Total General Obligation Bonds | **292.5** | 310.4 | 335.8 |
| Commerical Paper | **6.8** | 0.0 | 0.0 |
| Revenue Bonds | **8.7** | 13.2 | 17.9 |
| Total Long-Term Debt | **308.0** | 323.6 | 353.7 |
| Less Current Maturities | **(30.0)** | (22.7) | (29.7) |
| Long-term debt (net of unamortized premium/discount) | **$278.0** | $300.9 | $324.0 |

The Authority's total long-term debt decreased $15.6 million during the current fiscal year. The key factors in this decrease were reductions due to debt service payments of $22.4 million offset by new issuance of new commercial paper of $6.8 million

The Authority issued $9.0 million unlimited tax refunding bonds and used the proceeds, net of issuance cost, to establish an irrevocable escrow trust to provide for all future debt service requirement on the outstanding tax bonds, series 1994, that were refunded in December 2004. As a result, the Series 1994 Bonds are considered to be defeased and the liability for such bonds have been removed from the financial statements of the Authority in 2004. The Authority reduced its aggregate debt service payments by approximately $1.6 million over the next ten years.

The Authority maintains an AA+ rating from Fitch Ratings, Aa1 from Moody's Investors Service, Inc., and AA+ from Standard & Poor's Ratings Services on its general obligation bonds. The refunding revenue bonds were rated Aaa by Moody's Investors Service, Inc. and AAA by Standard & Poor's Rating Services.

Additional information on the Authority's long-term debt can be found in Note 8 on page 43 of this report.

**Economic Factors and Next Year's Budget and Rates**

- Inflationary trends in the Houston-Galveston area (increase of 3.6%) were higher than the all cities index (increase of 3.3%).
- With the lifting of the tariffs in late 2003, steel increased in 2004 to 2.6 million tons versus 1.4 million tons in 2003..
- Due to the overall market conditions, the total number of ships calling on Authority docks increased in 2004 (3,011) versus 2003 (2,875).
- The container ships that did call at the Authority's docks carried more tons in 2004 (12,952,000) versus 2003 (11,127,000).

All of the above factors were considered in preparing the Authority's budget for the 2005 fiscal year. The Authority increased tariffs an average of 3% effective January 3, 2005, and this increase contributed to an overall projected increase in operating revenues for 2005 of 9%.

**Requests for Information**

The financial report is designed to provide a general overview of the Authority's finances for all those with an interest in the Authority's finances. Questions concerning any of the information provided in this report, or requests for additional information, should be addressed to the Office of the Controller, Port of Houston Authority, 111 East Loop North, Houston, Texas 77029.

Port of Houston Authority
**Statements of Net Assets**
December 31, 2004 and 2003
(in thousands)

| | 2004 | 2003 |
|---|---|---|
| **Assets** | | |
| **Current Assets** | | |
| Cash and cash equivalents | **153,631** | 136,328 |
| Investments - current | **62,754** | 60,802 |
| Receivables (net of allowance for uncollectibles) | **17,346** | 17,068 |
| Inventories | **204** | 246 |
| Prepaids | **2,800** | 2,077 |
| Total Current Assets | **236,735** | 216,521 |
| **Restricted assets:** | | |
| Cash and cash equivalents | **56,255** | 63,290 |
| Property Tax Receivables | **24,797** | 31,024 |
| Investments - current | **63,155** | 72,245 |
| Investments - long term | **0** | 8,978 |
| Total Restricted assets | **144,207** | 175,537 |
| **Capital Assets (net of accumulated depreciation)** | | |
| Land | **233,938** | 168,167 |
| Buildings | **15,453** | 17,351 |
| Improvements other than buildings | **190,665** | 188,528 |
| Railroads | **33,512** | 33,617 |
| Machinery and equipment | **60,794** | 57,275 |
| Construction-in-progress | **124,497** | 142,470 |
| Total Capital Assets | **658,859** | 607,408 |
| **NonCurrent Assets** | | |
| Investments - long term | **16,582** | 19,116 |
| Deferred charges | **5,131** | 4,984 |
| Total Noncurrent assets | **21,713** | 24,100 |
| Total assets | **1,061,514** | 1,023,566 |
| **Liabilities** | | |
| Accounts payable and other current liabilities | **27,465** | 19,593 |
| Unearned revenue | **12,203** | 13,437 |
| Liabilities payable from restricted assets: | | |
| Current maturities of long-term debt | | |
| Commercial Paper | **6,800** | |
| Revenue bonds | **4,265** | 4,395 |
| Unlimited tax bonds | **18,940** | 18,345 |
| Accrued interest payable | | |
| Revenue bonds | **68** | 103 |
| Unlimited tax bonds | **3,530** | 3,891 |
| Contracts payable and accrued liabilities | **4** | 3 |
| Total current liabilities (payable from restricted assets) | **33,607** | 26,737 |
| Long-term debt, net of current maturities | **278,032** | 300,879 |
| Other noncurrent liabilities: | | |
| Due in more than one year | **19,308** | 21,276 |
| Total liabilities | **370,615** | 381,922 |
| **Net Assets** | | |
| Invested in capital assets, net of related debt | **431,595** | 397,063 |
| Restricted for: | | |
| Capital | **24,012** | 22,874 |
| Debt Service | **35,391** | 34,970 |
| Unrestricted | **199,901** | 186,737 |
| Total net assets | **690,899** | 641,644 |

See notes to financial statements

Port of Houston Authority

**Statements of Revenues, Expenses and Changes in Net Assets**

For the Years Ended December 31, 2004 and 2003

(in thousands)

| | 2004 | 2003 |
|---|---|---|
| **Operating revenues:** | | |
| Vessel and cargo services | **$116,506** | $101,085 |
| Rental of equipment and facilities | **15,878** | 14,977 |
| Grain elevator | **835** | 840 |
| Bulk materials | **2,348** | 2,978 |
| Other | **1,246** | 1,022 |
| Total | **136,813** | 120,902 |
| **Operating expenses:** | | |
| Maintenance and operation of facilities | **65,535** | 63,735 |
| General and administrative | **31,856** | 26,776 |
| Depreciation and amortization | **24,448** | 23,499 |
| Total | **121,839** | 114,010 |
| **Operating income** | **14,974** | 6,892 |
| **Nonoperating revenues (expenses):** | | |
| Interest income | **2,963** | 3,243 |
| Interest expense on bonds | **(808)** | (1,176) |
| Other, net | **5,106** | 8,207 |
| Total | **7,261** | 10,274 |
| **Income before nonoperating revenues (expenses) related to property taxes** | **22,235** | 17,166 |
| **Nonoperating revenues (expenses) related to property taxes:** | | |
| Property taxes | **33,088** | 37,396 |
| Interest income on unlimited tax bonds | **346** | (286) |
| Interest expense on unlimited tax bonds | **(8,217)** | (7,639) |
| Property tax expense | **(715)** | (931) |
| Other, net | **(391)** | (431) |
| Total nonoperating revenues (expenses) | **24,111** | 28,109 |
| **Income before contributions** | **46,346** | 45,275 |
| **Contribution from federal and state agency** | **2,909** | 870 |
| **Net income** | **49,255** | 46,145 |
| **Net assets, January 1** | **641,644** | 595,499 |
| **Net assets, December 31** | **$690,899** | $641,644 |

See notes to financial statements

Port of Houston Authority of Harris County, Texas

**Statements of Cash Flows**

For the Years Ended December 31, 2004 and 2003

(in thousands)

| | 2004 | 2003 |
|---|---|---|
| **Cash Flows from Operating Activities** | | |
| Cash Received from Customers | **$139,169** | $122,186 |
| Cash Paid to Suppliers for Goods and Services | **(40,710)** | (38,174) |
| Cash Paid to Employees for Services | **(30,151)** | (26,925) |
| Cash Paid for Employee Benefits | **(23,531)** | (22,402) |
| Cash from Other Services | **395** | 19,205 |
| Cash Paid for Other Purposes | **(532)** | (466) |
| Net Cash Provided by Operating Activities | **44,640** | 53,424 |
| **Cash Flows from Noncapital Financing Activities** | | |
| Repayment of Advances From Developer | **(1,398)** | (1,197) |
| Property Taxes Received | **38,941** | 34,405 |
| Property Tax Collection Expenses Paid | **(965)** | (1,063) |
| Grants Received from State and Federal Agencies | **0** | 45 |
| Net Cash Provided by Noncapital Financing Activities | **36,578** | 32,190 |
| **Cash Flows from Capital Financing Activities** | | |
| Grants Received from State and Federal Agencies | **1,837** | 825 |
| Proceeds from Issuance of Long - Term Debt | **15,800** | 7,060 |
| Issuance Costs of Long - Term Debt | **(117)** | (305) |
| Repayment of Long - Term Debt and Funding of Escrow | **(32,217)** | (30,207) |
| Interest on Long - Term Debt | **(16,357)** | (17,311) |
| Acquisition and Construction of Capital Assets | **(68,960)** | (49,855) |
| Proceeds from Retirement of Assets | **5,419** | 592 |
| Net Cash Used in Capital Financing Activities | **(94,595)** | (89,201) |
| **Cash Flows From Investing Activities** | | |
| Purchase of Investments | **(210,804)** | (208,193) |
| Proceeds from Maturities of Investments | **229,904** | 322,182 |
| Interest on Investments | **4,545** | 7,999 |
| Net Cash Provided by Investing Activities | **23,645** | 121,988 |
| **Net Increase in Cash and Cash Equivalents** | **10,268** | 118,401 |
| **Cash and Cash Equivalents, January 1** | **199,618** | 81,217 |
| **Cash and Cash Equivalents, December 31** | **$209,886** | $199,618 |
| **Current Cash and Cash Equivalents** | **$153,631** | $136,328 |
| **Restricted Cash and Cash Equivalents** | **$56,255** | $63,290 |

See notes to financial statements

Port of Houston Authority of Harris County, Texas
**Statements of Cash Flows - Continued**
For the Years Ended December 31, 2004 and 2003
(in thousands)

| | 2004 | 2003 |
|---|---|---|
| **Reconciliation of Operating Income to Net Cash Provided by Operating Activities** | | |
| Operating Income | **$14,974** | $6,892 |
| | | |
| Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities | | |
| Depreciation and Amortization | **24,448** | 23,499 |
| Provision for Doubtful Accounts | **120** | 120 |
| Miscellaneous Nonoperating Income (Expense) | **654** | 8,603 |
| | | |
| Change in Assets and Liabilities | | |
| Increase (Decrease) in Trade and Other Receivables | **1,515** | 507 |
| Decrease in Prepaid Expense | **(3,925)** | (25) |
| Decrease (Increase) in Inventory | **41** | 12 |
| Increase in Accounts Payable and Accrued Liabilities | **7,803** | 2,513 |
| Decrease (Increase) in Accrued Vacation and Sick Leave | **(45)** | 390 |
| Decrease in Deferred Gain | **(945)** | 10,913 |
| Net Cash Provided by Operating Activities | **$44,640** | **$53,424** |
| | | |
| Noncash Investing, capital, and financing activities: | | |
| Contributions of capital assets from government | **0** | 0 |
| Increase(Decrease) in fair value of investments | **(605)** | (1,115) |

See notes to financial statements

## 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, 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-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, in the opinion of management, 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 enforeceable, 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, 2004 and 2003 were $587.

The tax rates for the years ended December 31, 2004 and 2003 were $.01673 and $.02000 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 convenants.

(in thousands)

**Capital Assets**

Capital assets are defined by the Authority as assets with an initial, individual cost of more than $5 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 $6,053 and $6,613 in 2004 and 2003, 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 $195 per day.

**New Pronouncements**

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. The adoption of GASB No. 39 did not have a material impact on the financial statements of the Authority.

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.

In November 2003, the GASB issued Statement No. 42, "Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries." This statement will, among other things, establish accounting and financial reporting standards for the impairment of capital assets. Under this statement, a capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This statement is effective for periods beginning after June 15, 2004. Management of the Authority has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

GASB No. 43, "Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans," was issued May 2004 and establishes uniform financial reporting by state and local government entities for OPEB plans. This statement provides standards for measurement, recognition, and display of the assets, liabilities, and, where applicable, net assets and changes in net assets of such funds and for related disclosures. This statement is effective for periods beginning after December 15, 2005. Management of the Authority has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

In May 2004, the GASB issued Statement No. 44, "Economic Condition Reporting: The Statistical Section", an amendment of NCGA Statement 1. This statement establishes and modifies requirements related to the supplementary information presented in a statistical section. This statement applies to state and local governmental entities that prepare a statistical section that accompanies the basic financial statements. The provisions of this statement are effective for statistical sections prepared for periods beginning after June 15, 2005. Adoption of this statement is scheduled for the statistical sections prepared for the period beginning January 1, 2005.

GASB No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions" was issued July 2004. This statement addresses how state and local governments should account for and report their costs and obligations related to post-employment healthcare and other non-pension benefits (OPEB). The statement generally requires that state and local governmental employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. According to the phase in criteria, this statement is effective for periods beginning after December 15, 2006. Management of the Authority has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

In December 2004, the GASB issued Statement No. 46, "Net Assets Restricted by Enabling Legislation", an amendment of GASB Statement No. 24. The purpose of this statement is to help alleviate difficulties in identifying enabling legislation restrictions by clarifying that "legally enforceable" means that an external party – such as citizens, public interest groups, or the judiciary- can compel a government to use resources only for the purposes stipulated by the enabling legislation. The statement also requires governments to disclose in the notes to the financial statements the amount of net assets restricted by enabling legislation as of the end of the reporting period. Statement 46 is effective for periods beginning after June 15, 2005.

**Reclassifications -** Certain 2003 amounts have been reclassified to conform to the presentation.

## 2. Cash and Investments

The Authority's cash and cash equivalents balance of $209,886 and $199,618 as of December 31, 2004 and 2003, respectively, are maintained in demand accounts and mutual funds managed by a major fund manager. The bank balance at December 31, 2004 and 2003 was $211,231 and $201,829, 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 Reserve Bank of Chicago 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 security for which is guaranteed by an agency of the United States, and fully collateralized repurchase agreements. 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 2004 or 2003.

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:

(in thousands)

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, 2004 and 2003:

| | 2004 Categories | | | |
|---|---|---|---|---|
| | **1** | **2** | **3** | **Total** |
| **U.S. Government Agencies Securities** | $121,066 | $0 | $0 | $121,066 |
| **Commerical Paper** | 18,009 | | | 18,009 |
| **Municpal Bonds** | 3,416 | | | 3,416 |
| **Total** | $142,491 | $0 | $0 | $142,491 |

| | 2003 Categories | | | |
|---|---|---|---|---|
| | **1** | **2** | **3** | **Total** |
| **U.S. Government Agencies Securities** | $161,141 | $0 | $0 | $161,141 |
| **Total** | $161,141 | $0 | $0 | $161,141 |

(in thousands)

## 3. Receivables

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

| **Trade rceivables, net:** | **2004** | **2003** |
|---|---|---|
| Trade accounts | $16,413 | $16,213 |
| Damage claims | 676 | 1,606 |
| Less allowance for doubtful accounts | (1,076) | (1,319) |
| Trade accounts, net | 16,013 | 16,500 |
| **Other receivables:** | | |
| Accrued interest | 229 | 559 |
| Other | 1,104 | 9 |
| Total other receivables | 1,333 | 568 |
| **Total receivables, net** | $17,346 | $17,068 |

## 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, 2004 totaled $1,076 all classified as deferred charges. This transaction resulted in a deferred gain of approximately $2,998, which totaled $1,159 and $1,448 as of December 31, 2004 and 2003, respectively. This balance will be written off in equal installments over the life of the promissory note.

(in thousands)

## 5. Capital Assets

Capital asset activity for the year ended December 31, 2004 was as follows:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | |
| Land | $61,099 | $0 | $0 | $61,099 |
| Channel improvements | 107,068 | 66,296 | 525 | 172,839 |
| Construction-in-progress | 142,470 | 78,304 | 96,277 | 124,497 |
| Total capital assets, not being depreciated | 310,637 | 144,600 | 96,802 | 358,435 |
| Capital assets, being depreciated: | | | | |
| Buildings | 66,346 | 117 | 1 | 66,462 |
| Improvements other than buildings | 359,458 | 14,334 | 3 | 373,789 |
| Railroads | 55,144 | 1,149 | 18 | 56,275 |
| Machinery and equipment | 134,371 | 11,084 | 1,502 | 143,953 |
| Total capital assets, being depreciated | 615,319 | 26,684 | 1,524 | 640,479 |
| Less accumulated depreciation for: | | | | |
| Buildings | (48,995) | (2,015) | 1 | (51,009) |
| Improvements other than buildings | (170,930) | (12,197) | 3 | (183,124) |
| Railroads | (21,527) | (1,255) | 19 | (22,763) |
| Machinery and equipment | (77,096) | (7,452) | 1,389 | (83,159) |
| Total accumulated depreciation | (318,548) | (22,919) | 1,412 | (340,055) |
| Total capital assets, being depreciated, net | 296,771 | 3,765 | 112 | 300,424 |
| Total capital assets, net | $607,408 | $148,365 | $96,914 | $658,859 |

(in thousands)

Capital asset activity for the year ended December 31, 2003 was as follows:

| | Beginning Balance | Increases | Decreases | Ending Balance |
|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | |
| Land | $60,886 | $213 | $0 | $61,099 |
| Channel improvements | 106,645 | 1,135 | 712 | 107,068 |
| Construction-in-progress | 126,203 | 54,273 | 38,006 | 142,470 |
| Total capital assets, not be depreciated | 293,734 | 55,621 | 38,718 | 310,637 |
| Capital assets, being depreciated: | | | | |
| Buildings | 65,446 | 900 | 0 | 66,346 |
| Improvements other than buildings | 336,142 | 23,349 | 33 | 359,458 |
| Railroads | 55,000 | 144 | 0 | 55,144 |
| Machinery and equipment | 120,321 | 15,446 | 1,396 | 134,371 |
| Total capital assets, being depreciated | 576,909 | 39,839 | 1,429 | 615,319 |
| Less accumulated depreciation for: | | | | |
| Buildings | (46,954) | (2,041) | 0 | (48,995) |
| Improvements other than buildings | (158,867) | (12,074) | 11 | (170,930) |
| Railroads | (20,269) | (1,258) | 0 | (21,527) |
| Machinery and equipment | (72,385) | (6,107) | 1,396 | (77,096) |
| Total accumulated depreciation | (298,475) | (21,480) | 1,407 | (318,548) |
| Total capital assets, being depreciated, net | 278,434 | 18,359 | 22 | 296,771 |
| Total capital assets, net | $572,168 | $73,980 | $38,740 | $607,408 |

(in thousands)

## 6. Operating Leases

The Authority leases to others some of its land, buildings and improvements and cargo handling equipment. Cost of the assets under lease totaled $44,381 consisting of $5,502 in buildings, $5,209 in improvements, $1,103 of machinery and equipment and $32,567 of railroads with a total carrying value of $20,021 and current year depreciation of $948. As of December 31, 2004, 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 :

| | |
|---|---|
| 2005 | $ 12,149 |
| 2006 | 11,063 |
| 2007 | 8,255 |
| 2008 | 7,145 |
| 2009 | 6,299 |
| Thereafter | 81,486 |
| Total | $126,397 |

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, 2004, the monthly rental is $116. The Authority invoiced PTRA approximately $1,371 and $1,331 under this agreement in 2004 and 2003, 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, 2004 was approximately $2,848 and consisted of approximately $477 in current liabilities and approximately $2,394 in noncurrent liabilities. Future minimum lease payments are as follows for the years ended December 31:

(in thousands)

| | |
|---|---|
| 2005 | $ 599 |
| 2006 | 543 |
| 2007 | 488 |
| 2008 | 424 |
| 2009 | 405 |
| 2010 - 2012 | 957 |
| Total Lease Payments | 3,416 |
| Less: Amount representing interest | (568) |
| Present value of minimum lease payments | $ 2,848 |

Cost of assets machinery and equipment under lease are $6,430 with accumulated depreciation of $3,582 and current year depreciation of $477.

## 8. Long-Term Debt and NonCurrent Liabilities

**Changes in Long-Term Liabilities - 2004**

| | Beginning Balance | Additions | Deductions | Ending Balance | Current Portion | |
|---|---|---|---|---|---|---|
| Bonds Payable | | | | | | |
| Commercial Paper | $0 | $6,800 | $0 | $6,800 | $6,800 | |
| Revenue Bonds | 13,015 | 0 | 4,395 | 8,620 | 4,265 | |
| General Obligation Bonds | 306,245 | 9,000 | 27,345 | 287,900 | 18,940 | |
| Accretion, net | 3,001 | 481 | 0 | 3,482 | | |
| Less deferred amounts: | 1,358 | 225 | 348 | 1,235 | | |
| Total Bonds Payable | $323,619 | $16,506 | $32,088 | $308,037 | $30,005 | |
| Other noncurrent liabilities: | | | | | | |
| Capital Leases | $3,325 | $0 | $477 | $2,848 | $454 | (1 |
| Compensated Absences | 4,375 | 2,996 | 3,041 | 4,330 | 266 | (1 |
| Advances from Developer | 13,993 | 826 | 2,224 | 12,595 | 0 | |
| Other | 319 | | 64 | 255 | 0 | |
| Total other noncurrent liabilities | $22,012 | $3,822 | $5,806 | $20,028 | $720 | |

Port of Houston Authority of Harris County, Texas
**Notes to Financial Statements**
For the Years Ended December 31, 2004 and 2003
(in thousands)

**Changes in Long-Term Liabilities - 2003**

| | Beginning Balance | Additions | Deductions | Ending Balance | Current Portion | |
|---|---|---|---|---|---|---|
| Bonds Payable | | | | | | |
| Revenue Bonds | $17,335 | $0 | $4,320 | $13,015 | $4,395 | |
| General Obligation Bonds | 331,655 | 0 | 25,410 | 306,245 | 18,345 | |
| Accretion, net | 2,771 | 230 | 0 | 3,001 | | |
| Less deferred amounts: | 1,949 | 0 | 591 | 1,358 | | |
| Total Bonds Payable | $353,710 | $230 | $30,321 | $323,619 | $22,740 | |
| Other noncurrent liabilities: | | | | | | |
| Capital Leases | $3,802 | $0 | $477 | $3,325 | $477 | (1) |
| Compensated Absences | 3,985 | 2,978 | 2,588 | 4,375 | 259 | (1) |
| Advances from Developer | 15,190 | 1,600 | 2,797 | 13,993 | 0 | |
| Other | 320 | 0 | 1 | 319 | 0 | |
| Total other noncurrent liabilities | $23,297 | $4,578 | $5,863 | $22,012 | $736 | |

(1) Included in accounts payable and other noncurrent liabilities

**Long - Term Debt**

**Outstanding Long - Term Debt**

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

| | Original Issue | Interest Rate % | Issue Date | Maturity | December 31 2004 | December 31 2003 |
|---|---|---|---|---|---|---|
| **Commercial Paper:** | 6,800 | | 12/29/2005 | 2005 | **6,800** | **0** |
| **Revenue Bonds:** | | | | | | |
| Series 2002, Refunding | 22,285 | 2.00 - 5.00 | 02/20/02 | 2013 | **8,620** | **12,935** |
| **Special Purpose Revenue Bonds-** | | | | | | |
| Series 1964 | 1,900 | 2.50 | 07/01/64 | 2004 | **0** | **80** |
| Total Revenue Bonds | | | | | **8,620** | **13,015** |
| Add (Subtract) Unamortized Premiums/(Discounts) and Deferred Loss | | | | | **105** | **202** |
| Revenue Bonds, Net | | | | | **8,725** | **13,217** |
| **Unlimited Tax Refunding Bonds:** | | | | | | |
| Series 1997 * | 28,000 | 4.75 - 5.00 | 10/23/97 | 2013 | **15,935** | **19,120** |
| Series 1999B | 6,435 | 5.00 - 5.25 | 09/28/99 | 2009 | **3,050** | **3,700** |
| Series 2000B | 8,700 | 4.55 - 5.50 | 10/15/00 | 2011 | **5,180** | **5,960** |
| Series 2002B | 7,060 | 5.50 - 4.25 | 12/12/02 | 2013 | **4,810** | **5,905** |
| Series 2004 | 9,000 | 3.00 - 5.00 | 12/08/04 | 2016 | **9,000** | **0** |
| Total Unlimited Tax Refunding Bonds | | | | | **37,975** | **34,685** |
| Add (Subtract) Unamortized Premiums/(Discounts) and Deferred Loss | | | | | **788** | **752** |
| Series 1997 CAB, Accretion, net | | | | | **3,482** | **3,001** |
| Unlimited Tax Refunding Bonds, Net | | | | | **42,245** | **38,438** |
| **Unlimited Tax Port Improvement Bonds:** | | | | | | |
| Series 1994 | 15,000 | 6.50 - 8.50 | 12/01/94 | 2016 | **0** | **9,750** |
| Series 1995 | 12,000 | 4.90 - 6.90 | 11/01/95 | 2017 | **7,800** | **8,400** |
| Series 1996 | 42,000 | 5.50 - 7.50 | 04/01/96 | 2017 | **33,800** | **36,400** |
| Series 1997 | 28,000 | 4.80 - 5.375 | 07/09/97 | 2018 | **19,600** | **21,000** |
| Series 1998A | 81,000 | 3.80 - 5.00 | 11/17/98 | 2019 | **60,750** | **64,800** |
| Series 1998B | 7,000 | 3.40 - 5.40 | 11/17/98 | 2019 | **5,250** | **5,600** |
| Series 1999A | 14,000 | 5.5 | 09/28/99 | 2024 | **12,725** | **13,070** |
| Series 2000A | 12,000 | 4.25 - 5.10 | 10/15/00 | 2024 | **11,080** | **11,400** |
| Series 2001A | 17,000 | 5.0 | 11/01/01 | 2026 | **16,410** | **16,860** |
| Series 2001B | 70,000 | 4.00 - 5.00 | 11/01/01 | 2026 | **66,510** | **68,280** |
| Series 2002 A | 16,000 | 3.00 - 5.00 | 12/12/02 | 2027 | **16,000** | **16,000** |
| Total Unlimited Tax Port Improvement Bonds | | | | | **249,925** | **271,560** |
| Add Unamortized Premiums/(Discounts) | | | | | **342** | **404** |
| Unlimited Tax Port Improvement Bonds, Net | | | | | **250,267** | **271,964** |
| Total Long-Term Debt | | | | | **308,037** | **323,619** |
| Less Current Maturites | | | | | **(30,005)** | **(22,740)** |
| **Long - Term Debt** (net of unamortized premium/(discount)) | | | | | **$278,032** | **$300,879** |

* The Refunding Bonds, Series 1997A, consist of $13,450,000 Current Interest Bonds at 4.75 - 5.00 to mature 2000 - 2013 and $ 5,966,611 Capital Appreciation Bond at 4.80 - 4.85 to mature 2006 - 2007.

(in thousands)

The Authority periodically issues long term debt for the purpose of improving the facilities of the Authority, improve marine safety, and enhance environmental protection. At December 31, 2004, 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. At December 31, 2004, 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. During 2003, the Authority certified that a necessity existed for the issuance of up to $150,000 of the remaining authorized but not issued Unlimited Tax Bonds in the form of commercial paper notes. As of December 31, 2004, $6,800 in commercial paper has been issued.

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 2004 and 2003 were 1,059% and 861% 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, 2004 are as follows:

| | Bond Principal | | | Bond Interest | | | |
|---|---|---|---|---|---|---|---|
| Year Ending December 31 | Comm Paper | Revenue | Unlimited Tax | Comm Paper | Revenue | Unlimited Tax | Total |
| 2005 | $6,800 | $4,265 | $18,940 | $132 | $307 | $14,320 | $44,764 |
| 2006 | | 4,355 | 16,710 | | 101 | 15,705 | 36,871 |
| 2007 | | | 16,485 | | | 15,072 | 31,557 |
| 2008 | | | 18,695 | | | 11,981 | 30,676 |
| 2009 | | | 18,765 | | | 11,046 | 29,811 |
| 2010-2014 | | | 78,380 | | | 42,734 | 121,114 |
| 2015-2019 | | | 67,500 | | | 23,473 | 90,973 |
| 2020-2024 | | | 37,455 | | | 9,825 | 47,280 |
| 2025-2027 | | | 14,970 | | | 1,228 | 16,198 |
| | $6,800 | $8,620 | $287,900 | $132 | $408 | $145,384 | $449,244 |

(in thousands)

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.

**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 $20,250 and $43,670 as of December 31, 2004 and 2003 respectively, according to information received from the trustees. No bond was written off as uncollectible during 2004.

Revenue Bonds Outstanding

| Receiving Entity | Date Issued | Interest Rate | Maturity Date | Amount Issued | Balance |
|---|---|---|---|---|---|
| Mine Safety Applicance 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 | 12/01/84 | Variable | 12/01/04 | 40,000 | 0 |
| Cargill Inc. | 04/15/89 | 7.70% | 03/01/07 | 1,000 | 0 |
| Stolt Terminals (Houston) | 01/11/89 | Variable | 01/15/14 | 9,600 | 0 |
| Total | | | | $70,850 | $20,250 |

**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. The outstanding balance of the defeased unlimited tax bonds for December 31, 2004 and December 31, 2003 was $54,560 and $45,560 respectively.

(in thousands)

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 was refunded in January 2003. The Series 1992 bonds were considered to be defeased and the liability for such bonds were removed from the financial statements of the Authority in 2003. A gain of $15 was 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 | (57) | |
| Total | 7,153 | |
| Accrued interest payable | (108) | (7,045) |
| Deferred gain on refunding | | $ 15 |

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.

During 2004, the Authority issued $9,000 of unlimited tax 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 tax bonds, Series 1994 that were refunded in December 2004. The Series 1994 tax improvement bonds were considered to be defeased and the liability for such bonds were removed from the financial statements of the Authority in 2004. The outstanding balance of the defeased bonds were $9,000. A gain of $0 was realized on the refunding. The gain was determined as follows:

| | | |
|---|---|---|
| Principal balance of refunded bonds | | $9,000 |
| Less: | | |
| Total payments to trustee: | | |
| Face amount of refunding issue | $ 9,000 | |
| Premium received | 327 | |
| Issuance Costs | (195) | |
| Total | 9,132 | |
| Accrued interest payable | (132) | ( 9,000) |
| Deferred gain on refunding | | $ -0- |

The Authority reduced its aggregate debt service payments by approximately $1,556 over the next twelve years and obtained an economic gain (the difference between the present values of the old and new debt service payments) of approximately $1,276.

### Bond Restrictions

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, 2004 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. The liability for construction and operating advances amounted to approximately $12,595 and $13,993 at December 31, 2004 and 2003, respectively. All such advances are to 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 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 recorded $19,900 in advances from the developer at the time the new agreement was signed and has recorded an additional $1,600 in possible repayments during 2003 since at that time it was determined that future net revenues would be sufficient to pay all of the existing advances. The repayments during the 12 months ending December 31, 2004 and 2003 were approximately $2,224 and $2,797, 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, 2004 and 2003 was $23,170 (84% of the total payroll of $27,661) and $21,969 (81% of total payroll of $27,106), 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.

(in thousands)

**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.

**Actuarial Valuation Method**

| | | | |
|---|---|---|---|
| Actuarial Valuation Date | 08/01/04 | 08/01/03 | 08/01/02 |
| 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.

(in thousands)

**Plan Statistics**
**For Plan Years July 31, 2004, 2003, and 2002**
**Actuarial Valuation Report As of August 1, 2004, 2003, and 2002**

| | 2004 | % Covered Payroll | 2003 | % Covered Payroll | 2002 | % Covered Payroll |
|---|---|---|---|---|---|---|
| Actuarial Determined Employer Contribution Normal Cost | $1,559 | 6.7% | $1,482 | 6.7% | $1,334 | 6.6% |
| Annual Pension Cost | $6,983 | | $6,916 | | $3,229 | |
| % 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, 2004, 251 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, 2004 and 2003, the cost of retiree health benefits, recorded on a pay-as-you-go basis and net of contributions from retirees, was $2,014 and $1,754, respectively. Retiree life benefit costs for 2004 and 2003 were $19 and $19 respectively.

(in thousands)

## 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, 2004, the Authority was insured for the following loss limitations:

| | Workers' Compensation | General Liability | Automobile Liability |
|---|---|---|---|
| Per Accident | $200 | | |
| Bodily Injury | | | |
| Each Person | | | $100 |
| Each Accident | | $200 | $200 |
| Property Damage | | $100 | $100 |

The Authority's insurance policy also includes a maximum loss liability provision of $5,005 for the period from March 1, 2004 through March 1, 2005. Settled claims did not exceed the insurance coverage during the last three fiscal years.

The claims liability of $340 reported at December 31, 2004, 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.

(in thousands)

Changes in claim liability amounts in fiscal years 2004 and 2003 were as follows:

| | **2004** | 2003 |
|---|---|---|
| Unpaid claims and claim adjustment Expenses at beginning of year | **$159** | $37 |
| Incurred claims and claim adjustment expenses: | | |
| Provision for insured events of the current year | **676** | 403 |
| Changes in provision for insured events of prior years | **376** | 518 |
| Total incurred claims and claim adjustment expenses | **1052** | 921 |
| Payments: | | |
| Claims and claim adjustment expenses attributable to insured events of the current year | **350** | 168 |
| Claims and claim adjustment refunds attributable to insured events of prior ears | **521** | 631 |
| Total payment | **871** | 799 |
| Total unpaid claims and claim adjustment Expenses at year end | **$340** | $159 |

## 13. Commitments and Contingencies

### Commitments

At December 31 2004 the Authority had committed approximately $14,000 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.

In 1998 the Authority was sued in state court by plaintiff companies that own pipelines crossing the Houston Ship Channel at various points. The Authority subsequently removed the action to federal district court. The U.S. Army Corps of Engineers was also a defendant. The plaintiffs alleged that the Authority should bear the cost of removal or relocation of their pipelines in connection with widening and deepening of the Houston Ship Channel. In 2002, the district court entered judgment against the Authority concluding that the Authority, and not the pipeline companies, was responsible for the cost of pipeline removal or relocation. On January 30, 2004, the Fifth Circuit unanimously vacated the district court's order and rendered judgment in favor of the Authority and the U.S. Army Corps of Engineers. On April 1, 2004, the Fifth Circuit denied the pipelines' petition for rehearing, and on October 4, 2004 the U. S. Supreme Court denied plaintiffs' petition for writ of certiorari, concluding this matter.

**Required Supplementary Information**

**Port of Houston Authority Restated Retirement Plan**
**Schedule of Funding Progress**
(unaudited)

| | | | | |
|---|---|---|---|---|
| a) | Actuarial Valuation Date | 8/01/04 | 08/01/03 | 08/01/02 |
| b) | Actuarial Value of Assets | $74,868 | $66,992 | $59,638 |
| c) | Actuarial Accrued Liability (AAL) | $87,332 | $83,562 | $80,188 |
| d) | Unfunded (Overfunded) Actuarial Accrued Liability (UAAL) (c-b) | $12,464 | $16,570 | $20,550 |
| e) | Funded Ratio (b/c) | 85.7% | 80.2% | 74.4% |
| f) | Annual Covered Payroll (Actuarial) | $23,170 | $21,969 | $20,257 |
| g) | UAAL as a % of Covered Payroll (d/f) | 53.8% | 75.4% | 101.4% |

## APPENDIX B

### BOOK-ENTRY-ONLY SYSTEM

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants ("Direct Participants") deposit with DTC. DTC holds and provides asset servicing for over two million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, and trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: "AAA". The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for such purchases on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system described herein is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices will be sent to DTC. If less than all of the Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede

& Co.'s consenting or voting rights to those Direct Participants to whose accounts Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions, and dividend payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Authority or the Trustee, on each payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, Bonds are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bonds will be printed and delivered.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the Authority believes to be reliable, but the Authority nor the Underwriter takes no responsibility for the accuracy thereof.

* * *

# APPENDIX C

## FORM OF BOND COUNSEL OPINIONS

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ANDREWS
ATTORNEYS KURTH LLP

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__________, 2005

WE HAVE ACTED as Bond Counsel for Port of Houston Authority of Harris County, Texas (the "Authority") in connection with an issue of bonds (the "Bonds") described as follows:

> PORT OF HOUSTON AUTHORITY OF HARRIS COUNTY, TEXAS, UNLIMITED TAX REFUNDING BONDS, SERIES 2005A (AMT), dated August 1, 2005, in the aggregate principal amount of $36,665,000 maturing on October 1 in each year from 2014 through and including 2019 and in the year 2023. The Bonds are issuable in fully registered form only, in denominations of $5,000 or integral multiples thereof, bear interest, are subject to redemption prior to maturity and may be transferred and exchanged as set out in the Bonds and in the orders (the "Orders") adopted by the Port Commission of the Authority and the Commissioners Court of Harris County, Texas (the "County") authorizing their issuance.

WE HAVE ACTED as Bond Counsel for the sole purpose of rendering an opinion with respect to the legality and validity of the Bonds under the Constitution and laws of the State of Texas and with respect to the exclusion of interest on the Bonds from gross income under federal income tax law. In such capacity we have examined the Constitution and laws of the State of Texas; federal income tax law; and a transcript of certain certified proceedings pertaining to the issuance of the Bonds and the bonds (the "Refunded Bonds") and notes (the "Refunded Notes" and, together with the Refunded Bonds, the "Refunded Obligations") that are being refunded with the proceeds of the Bonds, as described in the Orders. The transcript contains certified copies of certain proceedings of the Authority, JPMorgan Chase Bank, National Association (the "Escrow Agent"); the report (the "Report") of Grant Thornton LLP, which verifies the sufficiency of the deposits made with the Refunded Bonds Escrow Agent for the refunding of the Refunded Bonds, and the mathematical accuracy of certain computations of the yield on the Bonds and the obligations acquired with the proceeds of the Bonds; certain certifications and representations and other material facts within the knowledge and control of the Authority, upon which we rely; and certain other customary documents and instruments authorizing and relating to the issuance of the Bonds and the firm banking and financial arrangements for the discharge and final payment of the Refunded Bonds. We have also examined executed Bond No. R-1.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the Authority or the disclosure thereof in connection with the sale of the Bonds. Our role in connection with the Authority's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

BASED ON SUCH EXAMINATION, it is our opinion as follows:

(1) The transcript of certified proceedings evidences complete legal authority for the issuance of the Bonds in full compliance with the Constitution and laws of the State of Texas presently in effect; the Bonds constitute valid and legally binding obligations of the Authority enforceable in accordance with the terms and conditions thereof, except to the extent that the rights and remedies of the owners of the Bonds may be limited by laws heretofore or hereafter enacted relating to bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting the rights of creditors of political subdivisions and the exercise of judicial discretion in appropriate cases; and the Bonds have been authorized and delivered in accordance with law;

(2) The Bonds are payable, both as to principal and interest, from the receipts of an annual ad valorem tax levied, without limit as to rate or amount, upon taxable property located within the County, which taxes have been pledged irrevocably to pay the principal of and interest on the Bonds;

(3) The escrow agreement between the Authority and the Escrow Agent (the "Escrow Agreement") has been duly executed and delivered and constitutes a binding and enforceable agreement in accordance with its terms; the establishment of the Escrow Fund pursuant to the Escrow Agreement and the deposits made therein constitute the making of firm banking and financial arrangements for the discharge and final payment of the Refunded Bonds; in reliance upon the accuracy of the calculations contained in the Report, the Refunded Bonds, having been discharged and paid, are no longer outstanding and the lien on and pledge of ad valorem taxes as set forth in the order authorizing their issuance will be appropriately and legally defeased; the holders of the Refunded Bonds may obtain payment of the principal of, redemption premium, if any, and interest in the Refunded Bonds only out of the funds provided therefor now held in escrow for that purpose by the Escrow Agent pursuant to the terms of the Escrow Agreement; and therefore the Refunded Bonds are deemed to be fully paid and no longer outstanding, except for the purpose of being paid from the funds provided therefor in such Escrow Agreement.

ALSO BASED ON OUR EXAMINATION AS DESCRIBED ABOVE, it is our further opinion that, subject to the restrictions hereinafter described, interest on the Bonds will be excludable from gross income of the owners thereof for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), except with respect to interest on any Bond for any period during which such Bond is held by a "substantial user" of the facilities financed or refinanced by the Bonds or a "related person" thereto as provided in Section 147(a) of the Code. The Bonds will be treated as "private activity bonds" within the meaning of Section 141 of the Code. Interest on the Bonds will be an item of tax preference for purposes of determining the alternative minimum tax imposed on individuals and corporations.

The opinion set forth in the preceding paragraph is subject to the condition that the Authority comply with all requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issuance of the Bonds in order that interest thereon be, or continue to be, excluded from gross income for federal income tax purposes. The Authority has covenanted in its Order to comply with each such requirement. Failure to comply with certain of such requirements may cause the inclusion of interest on the Bonds in gross income for federal income tax purposes to be retroactive to the date of issuance of the Bonds. The Code and the existing regulations, rulings and court decisions thereunder, upon which the foregoing opinions of Bond Counsel are based, are subject to change, which could prospectively or retroactively result in the inclusion of the interest on the Bonds in gross income of the owners thereof for federal income tax purposes.

INTEREST ON all tax-exempt obligations, including the Bonds, owned by a corporation (other than an S corporation, a regulated investment company, a real estate investment trust (REIT), a real estate mortgage investment conduit (REMIC) or a financial asset securitization investment trust (FASIT)) will be included in such corporation's adjusted current earnings for purposes of calculating such corporation's alternative minimum taxable income. A corporation's alternative minimum taxable income is the basis on which the alternative minimum tax imposed by the Code is computed. Purchasers of Bonds are directed to the discussion entitled "TAX MATTERS" set forth in the Official Statement.

EXCEPT AS DESCRIBED ABOVE, we express no opinion as to any federal, state or local tax consequences under present law, or future legislation, resulting from the ownership of, receipt or accrual of interest on, or the acquisition or disposition of, the Bonds. Prospective purchasers of the Bonds should be aware that the ownership of tax-exempt obligations, such as the Bonds, may result in collateral federal income tax consequences to, among others, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, individuals who may otherwise qualify for the earned income tax credit and taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations and individuals otherwise qualified for the earned income tax credit. For the foregoing reasons, prospective purchasers should consult their tax advisors as to the consequences of investing in the Bonds.

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ANDREWS
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__________, 2005

WE HAVE ACTED as Bond Counsel for Port of Houston Authority of Harris County, Texas (the "Authority") in connection with an issue of bonds (the "Bonds") described as follows:

> PORT OF HOUSTON AUTHORITY OF HARRIS COUNTY, TEXAS, UNLIMITED TAX REFUNDING BONDS, SERIES 2005B (NON-AMT), dated August 1, 2005, in the aggregate principal amount of $62,485,000 maturing on October 1 in each year from 2012 through and including 2013 and in each year from 2019 through and including 2023. The Bonds are issuable in fully registered form only, in denominations of $5,000 or integral multiples thereof, bear interest, are subject to redemption prior to maturity and may be transferred and exchanged as set out in the Bonds and in the orders (the "Orders") adopted by the Port Commission of the Authority and the Commissioners Court of Harris County, Texas (the "County") authorizing their issuance.

WE HAVE ACTED as Bond Counsel for the sole purpose of rendering an opinion with respect to the legality and validity of the Bonds under the Constitution and laws of the State of Texas and with respect to the exclusion of interest on the Bonds from gross income under federal income tax law. In such capacity we have examined the Constitution and laws of the State of Texas; federal income tax law; and a transcript of certain certified proceedings pertaining to the issuance of the Bonds and the bonds (the "Refunded Bonds") and notes (the "Refunded Notes" and, together with the Refunded Bonds, the "Refunded Obligations") that are being refunded with the proceeds of the Bonds, as described in the Orders. The transcript contains certified copies of certain proceedings of the Authority, JPMorgan Chase Bank, National Association (the "Escrow Agent"); the report (the "Report") of Grant Thornton LLP, which verifies the sufficiency of the deposits made with the Refunded Bonds Escrow Agent for the refunding of the Refunded Bonds, and the mathematical accuracy of certain computations of the yield on the Bonds and the obligations acquired with the proceeds of the Bonds; certain certifications and representations and other material facts within the knowledge and control of the Authority, upon which we rely; and certain other customary documents and instruments authorizing and relating to the issuance of the Bonds and the firm banking and financial arrangements for the discharge and final payment of the Refunded Bonds. We have also examined executed Bond No. R-1.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the Authority or the disclosure thereof in connection with the sale of the Bonds. Our role in connection with the Authority's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

BASED ON SUCH EXAMINATION, it is our opinion as follows:

(1) The transcript of certified proceedings evidences complete legal authority for the issuance of the Bonds in full compliance with the Constitution and laws of the State of Texas presently in effect; the Bonds constitute valid and legally binding obligations of the Authority enforceable in accordance with the terms and conditions thereof, except to the extent that the rights and remedies of the owners of the Bonds may be limited by laws heretofore or hereafter enacted relating to bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting the rights of creditors of political subdivisions and the exercise of judicial discretion in appropriate cases; and the Bonds have been authorized and delivered in accordance with law;

(2) The Bonds are payable, both as to principal and interest, from the receipts of an annual ad valorem tax levied, without limit as to rate or amount, upon taxable property located within the County, which taxes have been pledged irrevocably to pay the principal of and interest on the Bonds;

(3) The escrow agreement between the Authority and the Escrow Agent (the "Escrow Agreement") has been duly executed and delivered and constitutes a binding and enforceable agreement in accordance with its terms; the establishment of the Escrow Fund pursuant to the Escrow Agreement and the deposits made therein constitute the making of firm banking and financial arrangements for the discharge and final payment of the Refunded Bonds; in reliance upon the accuracy of the calculations contained in the Report, the Refunded Bonds, having been discharged and paid, are no longer outstanding and the lien on and pledge of ad valorem taxes as set forth in the order authorizing their issuance will be appropriately and legally defeased; the holders of the Refunded Bonds may obtain payment of the principal of, redemption premium, if any, and interest in the Refunded Bonds only out of the funds provided therefor now held in escrow for that purpose by the Escrow Agent pursuant to the terms of the Escrow Agreement; and therefore the Refunded Bonds are deemed to be fully paid and no longer outstanding, except for the purpose of being paid from the funds provided therefor in such Escrow Agreement.

ALSO BASED ON OUR EXAMINATION AS DESCRIBED ABOVE, it is our further opinion that, subject to the restrictions hereinafter described, interest on the Bonds will be excludable from gross income of the owners thereof for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), except with respect to interest on any Bond for any period during which such Bond is held by a "substantial user" of the facilities financed or refinanced by the Bonds or a "related person" thereto as provided in Section 147(a) of the Code. The Bonds will be treated as "private activity bonds" within the meaning of Section 141 of the Code. Interest on the Bonds will be an item of tax preference for purposes of determining the alternative minimum tax imposed on individuals and corporations.

The opinion set forth in the preceding paragraph is subject to the condition that the Authority comply with all requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issuance of the Bonds in order that interest thereon be, or continue to be, excluded from gross income for federal income tax purposes. The Authority has covenanted in its Order to comply with each such requirement. Failure to comply with certain of such requirements may cause the inclusion of interest on the Bonds in gross income for federal income tax purposes to be retroactive to the date of issuance of the Bonds. The Code and the existing regulations, rulings and court decisions thereunder, upon which the foregoing opinions of Bond Counsel are based, are subject to change, which could prospectively or retroactively result in the inclusion of the interest on the Bonds in gross income of the owners thereof for federal income tax purposes.

INTEREST ON all tax-exempt obligations, including the Bonds, owned by a corporation (other than an S corporation, a regulated investment company, a real estate investment trust (REIT), a real estate mortgage investment conduit (REMIC) or a financial asset securitization investment trust (FASIT)) will be included in such corporation's adjusted current earnings for purposes of calculating such corporation's alternative minimum taxable income. A corporation's alternative minimum taxable income is the basis on which the alternative minimum tax imposed by the Code is computed. Purchasers of Bonds are directed to the discussion entitled "TAX MATTERS" set forth in the Official Statement.

EXCEPT AS DESCRIBED ABOVE, we express no opinion as to any federal, state or local tax consequences under present law, or future legislation, resulting from the ownership of, receipt or accrual of interest on, or the acquisition or disposition of, the Bonds. Prospective purchasers of the Bonds should be aware that the ownership of tax-exempt obligations, such as the Bonds, may result in collateral federal income tax consequences to, among others, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, individuals who may otherwise qualify for the earned income tax credit and taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations and individuals otherwise qualified for the earned income tax credit. For the foregoing reasons, prospective purchasers should consult their tax advisors as to the consequences of investing in the Bonds.

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## APPENDIX D

## SUMMARY OF TABLES AND SCHEDULES RELATED TO CONTINUING DISCLOSURE OF INFORMATION

| | | | | |
|---|---|---|---|---|
| Table 1 | — | AUTHORITY AD VALOREM TAXES | — | Table of Authority Tax Rates |
| Table 2 | — | AUTHORITY AD VALOREM TAXES | — | Table of Authority Taxable Values and Tax Rates |
| Table 3 | — | AUTHORITY AD VALOREM TAXES | — | Table of Authority Tax Levies, Collections, and Delinquencies |
| Table 4 | — | AUTHORITY AD VALOREM TAXES | — | Table of Principal Taxpayers |
| Table 5 | — | AUTHORITY AD VALOREM TAX DEBT | — | Table of Ad Valorem Tax Debt Comparisons |
| Table 6 | — | AUTHORITY AD VALOREM TAX DEBT | — | Table of Debt Service Requirements |
| Table 7 | — | THE AUTHORITY | — | Table of Physical Characteristics of the Port Facilities of the Authority |
| Table 8 | — | THE AUTHORITY | — | Financial Condition and Operations — Summary of Comparative Historical Balance Sheets |
| Table 9 | — | THE AUTHORITY | — | Financial Condition and Operations — Summary of Comparative Historical Operations |
| Table 10 | — | THE AUTHORITY | — | Table of Annual Cargo Amounts |
| Table 11 | — | INVESTMENTS | — | Current Investments — Schedule of Distribution of Authority Investments |

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## APPENDIX E

### Schedule of Refunded Bonds

Port of Houston Authority of Harris County, Texas
Unlimited Tax Refunding Bonds, Series 2005A (AMT)

| Issue | Maturity Date (October 1) | Refunded Principal Amount | Interest Rate | Redemption Price | Call Date (October 1) |
|---|---|---|---|---|---|
| Unlimited Tax Port Improvement Bonds, Series 1995 (AMT) | 2006 | $ 600,000 | 5.200% | 100 | 2005 |
| | 2007 | 600,000 | 5.300 | 100 | 2005 |
| | 2008 | 600,000 | 5.400 | 100 | 2005 |
| | 2009 | 600,000 | 5.500 | 100 | 2005 |
| | 2010 | 600,000 | 5.600 | 100 | 2005 |
| | 2011 | 600,000 | 5.650 | 100 | 2005 |
| | 2012 | 600,000 | 5.700 | 100 | 2005 |
| | 2013 | 600,000 | 5.750 | 100 | 2005 |
| | 2014 | 600,000 | 5.750 | 100 | 2005 |
| | 2015 | 600,000 | 5.750 | 100 | 2005 |
| | 2016 | 600,000 | 5.750 | 100 | 2005 |
| | 2017 | 600,000 | 5.750 | 100 | 2005 |
| | | $7,200,000 | | | |

Port of Houston Authority of Harris County, Texas
Unlimited Tax Refunding Bonds, Series 2005B (Non-AMT)

| Issue | Maturity Date (October 1) | Refunded Principal Amount | Interest Rate | Redemption Price | Call Date (October 1) |
|---|---|---|---|---|---|
| Unlimited Tax Port Improvement Bonds, Series 1997 (Non-AMT) | 2006 | $ 1,400,000 | 5.375% | N/A | N/A |
| | 2007 | 1,400,000 | 4.800 | N/A | N/A |
| | 2008 | 1,400,000 | 4.875 | 100 | 2007 |
| | 2009 | 1,400,000 | 5.000 | 100 | 2007 |
| | 2010 | 1,400,000 | 5.000 | 100 | 2007 |
| | 2011 | 1,400,000 | 5.100 | 100 | 2007 |
| | 2012 | 1,400,000 | 5.250 | 100 | 2007 |
| | 2013 | 1,400,000 | 5.250 | 100 | 2007 |
| | 2014 | 1,400,000 | 5.250 | 100 | 2007 |
| | 2015 | 1,400,000 | 5.250 | 100 | 2007 |
| | 2016 | 1,400,000 | 5.125 | 100 | 2007 |
| | 2017 | 1,400,000 | 5.125 | 100 | 2007 |
| | 2018 | 1,400,000 | 5.125 | 100 | 2007 |
| | | $18,200,000 | | | |

| Issue | Maturity Date (October 1) | Refunded Principal Amount | Interest Rate | Redemption Price | Call Date (October 1) |
|---|---|---|---|---|---|
| Unlimited Tax Port Improvement Bonds, Series 1998B (Non-AMT) | 2006 | $ 350,000 | 5.400% | N/A | N/A |
| | 2007 | 350,000 | 5.400 | N/A | N/A |
| | 2008 | 350,000 | 5.400 | N/A | N/A |
| | 2009 | 350,000 | 4.150 | 100 | 2008 |
| | 2010 | 350,000 | 4.250 | 100 | 2008 |
| | 2011 | 350,000 | 4.350 | 100 | 2008 |
| | 2012 | 350,000 | 4.400 | 100 | 2008 |
| | 2013 | 350,000 | 4.550 | 100 | 2008 |
| | 2014 | 350,000 | 4.600 | 100 | 2008 |
| | 2015 | 350,000 | 4.700 | 100 | 2008 |
| | *** | *** | *** | *** | *** |
| | 2017 | 700,000 | 4.800 | 100 | 2008 |
| | *** | *** | *** | *** | *** |
| | 2019 | 700,000 | 4.875 | 100 | 2008 |
| | | $4,900,000 | | | |

| Issue | Maturity Date (October 1) | Refunded Principal Amount | Interest Rate | Redemption Price | Call Date (October 1) |
|---|---|---|---|---|---|
| Unlimited Tax Port Improvement Bonds, Series 1999A (Non-AMT) | 2006 | $ 385,000 | 5.500% | N/A | N/A |
| | 2007 | 405,000 | 5.500 | N/A | N/A |
| | 2008 | 425,000 | 5.500 | N/A | N/A |
| | 2009 | 450,000 | 5.500 | N/A | N/A |
| | 2010 | 475,000 | 5.500 | 100 | 2009 |
| | 2011 | 500,000 | 5.500 | 100 | 2009 |
| | 2012 | 530,000 | 5.500 | 100 | 2009 |
| | 2013 | 560,000 | 5.500 | 100 | 2009 |
| | 2014 | 590,000 | 5.500 | 100 | 2009 |
| | 2015 | 620,000 | 5.500 | 100 | 2009 |
| | 2016 | 655,000 | 5.500 | 100 | 2009 |
| | 2017 | 690,000 | 5.500 | 100 | 2009 |
| | 2018 | 730,000 | 5.500 | 100 | 2009 |
| | 2019 | 770,000 | 5.500 | 100 | 2009 |
| | *** | *** | *** | *** | *** |
| | 2024 | 4,575,000 | 5.750 | 100 | 2009 |
| | | $12,360,000 | | | |

| Issue | Maturity Date (October 1) | Refunded Principal Amount | Interest Rate | Redemption Price | Call Date (October 1) |
|---|---|---|---|---|---|
| Unlimited Tax Port Improvement Bonds, Series 2000A (Non-AMT) | 2006 | $ 350,000 | 4.600% | N/A | N/A |
| | 2007 | 365,000 | 4.700 | N/A | N/A |
| | 2008 | 380,000 | 4.750 | N/A | N/A |
| | 2009 | 400,000 | 4.750 | N/A | N/A |
| | 2010 | 420,000 | 5.500 | N/A | N/A |
| | 2011 | 440,000 | 5.000 | 100 | 2010 |
| | 2012 | 465,000 | 5.000 | 100 | 2010 |
| | 2013 | 485,000 | 5.000 | 100 | 2010 |
| | 2014 | 510,000 | 5.100 | 100 | 2010 |
| | *** | *** | *** | *** | *** |
| | 2016 | 1,100,000 | 5.250 | 100 | 2010 |
| | *** | *** | *** | *** | *** |
| | 2020 | 2,595,000 | 5.750 | 100 | 2010 |
| | *** | *** | *** | *** | *** |
| | 2024 | 3,235,000 | 5.500 | 100 | 2010 |
| | | $10,745,000 | | | |

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**APPENDIX F**
**FINANCIAL GUARANTY INSURANCE POLICY**
**MBIA Insurance Corporation**
**Armonk, New York 10504**

Policy No. [NUMBER]

MBIA Insurance Corporation (the "Insurer"), in consideration of the payment of the premium and subject to the terms of this policy, hereby unconditionally and irrevocably guarantees to any owner, as hereinafter defined, of the following described obligations, the full and complete payment required to be made by or on behalf of the Issuer to [PAYING AGENT/TRUSTEE] or its successor (the "Paying Agent") of an amount equal to (i) the principal of (either at the stated maturity or by any advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Obligations (as that term is defined below) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed hereby shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration, unless the Insurer elects in its sole discretion, to pay in whole or in part any principal due by reason of such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law. The amounts referred to in clauses (i) and (ii) of the preceding sentence shall be referred to herein collectively as the "Insured Amounts." "Obligations" shall mean:

**[PAR]**
**[LEGAL NAME OF ISSUE]**

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Insurer from the Paying Agent or any owner of an Obligation the payment of an Insured Amount for which is then due, that such required payment has not been made, the Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such Insured Amounts which are then due. Upon presentment and surrender of such Obligations or presentment of such other proof of ownership of the Obligations, together with any appropriate instruments of assignment to evidence the assignment of the Insured Amounts due on the Obligations as are paid by the Insurer, and appropriate instruments to effect the appointment of the Insurer as agent for such owners of the Obligations in any legal proceeding related to payment of Insured Amounts on the Obligations, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners, or the Paying Agent payment of the Insured Amounts due on such Obligations, less any amount held by the Paying Agent for the payment of such Insured Amounts and legally available therefor. This policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Obligation.

As used herein, the term "owner" shall mean the registered owner of any Obligation as indicated in the books maintained by the Paying Agent, the Issuer, or any designee of the Issuer for such purpose. The term owner shall not include the Issuer or any party whose agreement with the Issuer constitutes the underlying security for the Obligations.

Any service of process on the Insurer may be made to the Insurer at its offices located at 113 King Street, Armonk, New York 10504 and such service of process shall be valid and binding.

This policy is non-cancellable for any reason. The premium on this policy is not refundable for any reason including the payment prior to maturity of the Obligations.

IN WITNESS WHEREOF, the Insurer has caused this policy to be executed in facsimile on its behalf by its duly authorized officers, this [DAY] day of [MONTH, YEAR].

**MBIA Insurance Corporation**

SPECIMEN

______________________________
President

Attest: ______________________________
Assistant Secretary

**DISCLOSURE OF GUARANTY FUND NONPARTICIPATION: In the event the Insurer is unable to fulfill its contractual obligation under this policy or contract or application or certificate or evidence of coverage, the policyholder or certificateholder is not protected by an insurance guaranty fund or other solvency protection arrangement.**

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**PORT OF HOUSTON AUTHORITY**

**OF**

**HARRIS COUNTY**
**(a political subdivision of the State of Texas having boundaries coterminous with Harris County)**

**UNLIMITED TAX REFUNDING BONDS, SERIES 2005A (AMT)**

**And**

**UNLIMITED TAX REFUNDING BONDS, SERIES 2005B (NON-AMT)**

**PORT COMMISSION**

James T. Edmonds ..................................................... Chairman

Kase L. Lawal ................................ Vice Chairman

Steve L. Phelps ............................... Commissioner

James W. Fonteno, Jr ........................ Commissioner

Jimmy Burke ................................... Commissioner

Cheryl Thompson-Draper ................. Commissioner

Janiece Longoria ............................... Commissioner

H. Thomas Kornegay ................................. Executive Director

Wade M. Battles ........................................ Managing Director

Erik A. Eriksson ............................................... General Counsel

Barbara J. Schott, CPA ................................... County Auditor

Jack Cato ..................................................... County Treasurer