

## Exhibit G: Financial Model Run Overview

One of the most important tools needed to evaluate the future governance alternatives for The Woodlands was the financial impact to the community. Early in Phase II of the process, the Finance Response Team of the GSC was charged with crafting a "Request for Qualifications" (RFQ) to solicit an expert who could address the financial impact to The Woodlands.

Over a year ago, Dr. Jim Gaines, faculty member of Texas A&M University, was selected as the GSC finance consultant. Dr. Gaines has intimate knowledge of The Woodlands and has partnered with the community in the past; this experience was critical for the GSC and played a large role in his selection. Over the past months, the Finance Response Team has worked with Dr. Gaines as he built a model which would assist the GSC in determining costs related to implementing various governance alternatives.

"The Gaines Model" is a comprehensive financial program that includes the budgets of entities such as The Woodlands Community Association, The Woodlands Association, The Woodlands Commercial Owners Association, Municipal Utility Districts, and Town Center Improvement District. Additionally, the budgets of four cities were utilized not only for purposes of reference for those services not currently provided in The Woodlands, but also for purposes of ensuring the projected governance alternative budgets for the project are in-line with existing cities of comparable size and demographic composition. The comparable cities selected for this model (and their associated per capita expenditures) were Sugar Land (\$1,122), Grand Prairie (\$873), Lewisville (\$749), and Plano (\$955). The comparable city average per capita expenditure is \$925. Further, the study commissioned by the Community Associations of The Woodlands from law enforcement consultant and former police chief of Chattanooga, TN, Jimmie Dotson, was also utilized in this analysis to determine the cost of potential enhanced law enforcement services.

While the cost estimates are based on many factors and assumptions, there are some predictable figures we can rely on:

- We know what the costs are to provide current services in The Woodlands;
- We can confidently estimate what additional revenues can be realized under the different alternatives;
- We know what the per capita costs are to run a municipality based on the legal budgets of comparable cities;
- We know what the county spends and is anticipating to spend for services (such as law enforcement and maintaining the street network) that will be discontinued/diminished under an incorporation scenario.

The majority of the figures generated (expressing the costs and expenditures of the two governance alternatives) come from these factors. Therefore, we can be quite confident that the results generated by the financial model are representative unless the *assumptions* and *service levels* are dramatically changed.

While the assumptions behind the individual line items and figures can be debated endlessly, the product produced provides a conservative and base-line analysis for purposes of recommending a governance alternative(s) to pursue.

### WHAT ARE SOME OF THE DIFFERENCES BETWEEN THE ALTERNATIVES?

#### As Is (for purposes of comparison only)

- Association assesses property owners and provides municipal-type services—assessments are not federally tax-deductible;
- Municipal Utility Districts (MUDs) tax property owners and provide water/sewer/drainage services—MUD taxes are federally tax-deductible;
- No sales or property tax revenues are collected by Association.

#### Alternative 1: Public Service District

- A public service district is created that would assess sales and property taxes to fund services currently provided by the Associations and to enhance law enforcement—district property taxes would be federally tax-deductible;
- MUDs remain intact;
- Maximum allowed local sales tax revenues are captured (1% in TCID, 2% elsewhere);
- Role of Associations and their associated assessments rates will be greatly diminished.

**Alternative 2: Incorporation**

- A city is established to assess sales and property taxes to fund the replacement of services provided by the Associations and MUDs, as well as to fund services a city is obligated to provide according to state law—city property taxes would be federally tax-deductible;
- Maximum allowed local sales tax revenues are captured (1% in TCID, 2% elsewhere);
- Additional revenue streams are made available such as fines, fees and service charges;
- Some services previously provided by the county would be the responsibility of city, most notably street maintenance and law enforcement;
- Water/sewer/drainage provided by the city through utilization of property tax and service fee funding;
- Role of Associations and their respective assessment rates will be greatly diminished.

**WHAT WOULD CHANGE?**

	Significant New Revenues	Significant New Expenditures and/or Services	Services Lost or Diminished
<b>Public Service District</b>	<ul style="list-style-type: none"> <li>• Sales taxes</li> <li>• Potential grants</li> <li>• Property tax</li> </ul>	<ul style="list-style-type: none"> <li>• Enhanced law enforcement</li> <li>• One time conversion costs</li> </ul>	None
<b>Incorporation</b>	<ul style="list-style-type: none"> <li>• Sales taxes</li> <li>• Franchise fees</li> <li>• Fines and other fees/permits</li> <li>• Potential grants</li> <li>• Property tax</li> </ul>	<ul style="list-style-type: none"> <li>• Creation of a municipal police department</li> <li>• Municipal street maintenance and construction</li> <li>• Municipal court</li> <li>• Additional municipal capital expenditures</li> <li>• One time conversion costs</li> </ul>	<ul style="list-style-type: none"> <li>• Law enforcement services from Sheriff</li> <li>• County street maintenance and construction</li> <li>• Animal control</li> <li>• Some social services</li> <li>• Mosquito control</li> </ul>

**MODEL ASSUMPTIONS**

- Service levels of the Public Service District are at the “As Is” level and have been transferred dollar for dollar from the Associations into the district with the exception of enhanced law enforcement.
- Upon incorporation, counties will only provide the services required by law.
- General street maintenance costs for incorporation have been estimated at \$2 million per year based on county current expenditures.
- Street construction debt for incorporation has been set at \$10 million based on county’s capital improvement program.
- Recognizing that it will take several years for incorporation to become fully operational, “Year 5” is considered the stabilized and realistic expense projection for incorporation.
- Additional costs will be incurred in the first three years to augment lost county services at the point of incorporation which are not currently included in the model.
- The weighted MUD average tax rate has been conservatively estimated to decrease by 3 percent per year. This is based on a 10 percent average decrease over the past six years as debt is retired.
- Conversion costs for the public service district and incorporation have been estimated at \$500,000 and \$3.6 million respectively.
- Costs associated with providing water/sewer/drainage services by the city have been captured partially utilizing property tax revenues and supplementing with increased service fees.
- The Village of Creekside Park in Harris County (and the associated MUDs) while included in the governance project and any governance alternative selected, were not included in the financial model.
- Costs related to the future transition from ground water to surface water was not included as this would impact both alternatives.
- Communities already incorporated into a city (such as parts of Grogan’s Forest in Shenandoah and Windsor Lakes in Conroe) are not included in the analysis.
- Both alternatives assume an increased sales tax rate of 1% in TCID and 2% throughout the rest of the rest of The Woodlands. Because consumer spending varies per household, each resident will have to evaluate their spending habits to determine the individual budgetary impact of the increased sales tax.

**Table 1: Year Five Consolidated Operating Budget <sup>1</sup>**

	Public Service District		Incorporation		Per Capita Average of Comparative Cities
	Total	Per Capita Cost	Total	Per Capita Cost	
Sales Tax Rate	TCID 1%, Elsewhere 2%		TCID 1%, Elsewhere 2%		n/a
Property Tax Rate	0.2450		0.7000		\$0.47
Assessed Value Per Capita	\$98,592		\$98,592		\$69,660
<b><u>Operating Revenues <sup>2</sup></u></b>					
Property Tax	\$22,378,080	\$214	\$37,862,355	\$362	\$193
Sales Tax	\$27,441,484	\$262	\$27,441,484	\$262	\$193
Municipal Court (Fines/Sanctions)	\$0	\$0	\$3,634,532	\$35	\$32
Fines & Penalties	\$0	\$0	\$70,391	\$1	\$1
Licenses & Permits	\$0	\$0	\$1,864,407	\$18	\$16
Pool & Recreation Revenues	\$766,778	\$7	\$766,778	\$7	\$25
Charges for Services	\$0	\$0	\$7,294,819	\$70	\$63
Total Franchise Tax Revenues	\$0	\$0	\$6,172,098	\$59	\$48
Grants and Loans	\$0	\$0	\$3,642,920	\$35	\$6
Interest Income & Earnings	\$573,875	\$5	\$313,754	\$3	\$15
Other	\$451,600	\$4	\$451,600	\$4	\$0
Miscellaneous	\$146,449	\$1	\$2,785,033	\$27	\$48
<i>Comparative City Other</i>					\$227
<b>TOTAL OPERATING REVENUES</b>	<b>\$51,758,266</b>	<b>\$495</b>	<b>\$92,300,171</b>	<b>\$883</b>	<b>\$867</b>
<b><u>Operating Expenses <sup>2</sup></u></b>					
Administrative Services	\$3,956,369	\$38	\$10,345,880	\$99	\$219
Public Safety	\$18,724,656	\$179	\$34,431,191	\$329	\$315
Building Services	\$250,000	\$2	\$2,365,273	\$23	\$27
Planning & Development	\$2,407,195	\$23	\$4,864,127	\$47	\$31
Parks & Public Works	\$21,331,055	\$204	\$30,238,973	\$289	\$152
Human & Cultural Services	\$2,447,402	\$23	\$5,392,768	\$52	\$180
Contingency	\$2,455,834	\$23	\$4,381,911	\$42	\$0
<b>TOTAL OPERATING EXPENSES</b>	<b>\$51,572,511</b>	<b>\$493</b>	<b>\$92,020,123</b>	<b>\$880</b>	<b>\$924</b>
<b>Surplus (Deficit)</b>	<b>\$185,755</b>	<b>\$2</b>	<b>\$280,048</b>	<b>\$3</b>	<b>(\$57)</b>

Comparative cities used a beginning fund balance to offset their operating deficit, an element not reflected in this consolidated budget.

<sup>1</sup> Includes both debt service and operating expenses

<sup>2</sup> For purposes of direct comparisons with Texas cities, debt service expenses and corresponding revenues are not included.

- WCA: The Woodlands Community Association
- TWA: The Woodlands Association
- WCOA: The Woodlands Commerical Owners Association
- PSD: Public Service District
- TCID: Town Center Improvement District

# What does this mean for the \$250,000 Homeowner?

The following table lists all scenarios and net homeowner costs based on the test case homeowner in years three and five. Based on the phasing-in of services and facilities, year five indicates the long-term ramifications of each Governance Alternative.

**Table 2: Years Three and Five Governance Alternative Comparison for \$250,000 Homeowner in 28% Tax Bracket**

	As is		Public Service District <sup>3</sup>		Incorporation <sup>3</sup>	
	year 3	5	3	5	3	5
Public Service District (PSD)	\$0	\$0	\$813	\$613	\$0	\$0
Woodlands City	\$0	\$0	\$0	\$0	\$2,125	\$1,750
MUD (weighted avg)	\$737	\$693	\$737	\$694	\$0	\$0
WCA (2006)	\$1,138	\$1,138	\$0	\$0	\$0	\$0
TWA (2006)	\$1,225	\$1,225	\$0	\$0	\$0	\$0
WCOA (2006)	\$975	\$975	\$0	\$0	\$0	\$0
Water/Sewer Fees	\$394	\$394	\$394	\$394	\$884	\$864
Income Tax savings @ 28%	-\$206	-\$194	-\$434	-\$366	-\$595	-\$490
<b>WCA resident cost</b>	<b>\$2,063</b>	<b>\$2,031</b>	<b>\$1,510</b>	<b>\$1,334</b>	<b>\$2,414</b>	<b>\$2,124</b>
<b>TWA resident cost</b>	<b>\$2,150</b>	<b>\$2,118</b>	<b>\$1,510</b>	<b>\$1,334</b>	<b>\$2,414</b>	<b>\$2,124</b>
<b>WCOA resident cost</b>	<b>\$1,900</b>	<b>\$1,868</b>	<b>\$1,510</b>	<b>\$1,334</b>	<b>\$2,414</b>	<b>\$2,124</b>
<b>Average As-Is resident cost</b>	<b>\$2,038</b>	<b>\$2,006</b>				

**Table 3. Actual Net Tax Differences Among Governance Alternatives for \$250,000 Homeowner in Year 5**

	Per Household Cost in Dollars <sup>a</sup>	Cost Difference from Avg As-Is	Cost Difference from Public Service District	Cost Difference from City without TCID
WCA As-Is	\$2,031		\$697	-\$93
TWA As-Is	\$2,118		\$784	-\$6
WCOA As-Is	\$1,868		\$534	-\$256
Public Service District	\$1,334	-\$672		-\$790
Incorporation	\$2,124	\$118	\$790	

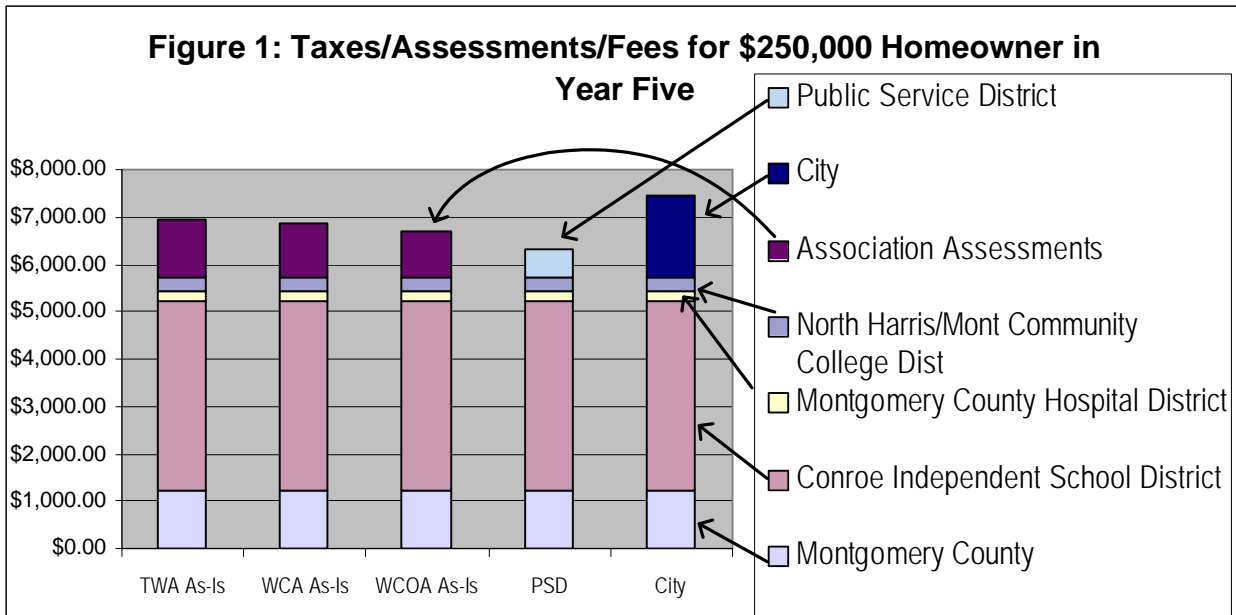
**Table 4: Percent Differences Between Year 5 Governance Alternatives for \$250,000 Homeowner**

(excludes additional sales taxes paid by homeowner under special public services district and both incorporation scenarios)

Public Service District is **34% less** than Average As-Is

Incorporation is **6% more** than Average As-Is \*

Incorporation is **60% more** than Public Service District \*



<sup>3</sup> does not include additional sales taxes paid by homeowner

<sup>a</sup> assumes 10,000 gallons/month usage

<sup>b</sup> includes costs of MUDs and any other services provided, but does not include County, CISD, NHMCCD and MCHD taxes.

\*Town Center Improvement District (TCID) remains in operations