

**HARRIS COUNTY  
IMPROVEMENT DISTRICT NO. 1**

**SINGLE AUDIT REPORT**

**Fiscal Year Ended June 30, 2012**



# HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

## SINGLE AUDIT REPORT

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON  
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

To the Board of Directors  
Harris County Improvement District No. 1  
Houston, Texas

We have audited the financial statements of the governmental activities and each major fund of Harris County Improvement District No. 1's (the "District") as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements and have issued our report thereon dated November 30, 2012. We conducted our audit 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.

***Internal Control over Financial Reporting***

Management of the District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting. Finding #12-01 and #12-02. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedules of findings and questioned costs as item #12-03.

This report is intended solely for the information and use of the Board of Directors, management, others within the organization, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Whitley Penn LLP". The signature is written in a cursive, flowing style.

Houston, Texas  
November 30, 2012

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT  
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM  
AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE  
WITH OMB CIRCULAR A-133**

To the Board of Trustees  
Harris County Improvement District No. 1  
Houston, Texas

***Compliance***

We have audited Harris County Improvement District No. 1's (the "District") compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2012. The District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the District's compliance with those requirements.

In our opinion, Harris County Improvement District No. 1 complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. However the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item #12-01.

***Internal Control over Compliance***

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

***Schedule of Expenditures of Federal Awards***

We have audited the financial statements of the governmental activities and each major fund of the District as of and for the year ended June 30, 2012, and have issued our report thereon dated November 30, 2012, which contained unqualified opinions on those financial statements. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the District's financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for the purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the financial statements as a whole.

This report is intended solely for the information and use of the Board of Directors, management, others within the organization, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Houston, Texas  
November 30, 2012



**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
*For the Year Ended June 30, 2012*

**I. Summary of Auditors' Results**

**Financial Statements**

Type of auditors' report issued	Unqualified
Internal control over financial reporting:	
Material weakness (es) identified?	No
Significant deficiency (ies) identified that are not considered to be material weaknesses?	Yes, #12-01 and #12-02
Noncompliance material to the financial statements noted?	No

**Federal Awards**

Internal controls over major programs:	
Material weakness (es) identified?	No
Significant deficiency (ies) identified that are not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with section .510(a) 2-7 of OMB Circular A-133	Yes, #12-03

Identification of Major Programs:

<b>Name of Federal Program</b>	<b>CFDA Number</b>
<b>Federal Transit Administration</b>	
Federal Transit Cluster	
Federal Transit – Capital Investment	20.500
Federal Transit – Formula Grants	20.507
Dollar Threshold Considered Between Type A and Type B Federal Programs	\$300,000
Auditee qualified as low-risk auditee?	Yes

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
*For the Year Ended June 30, 2012 (continued)*

**II. Financial Statement Findings**

**Finding #12-01 Journal Entry Review**

**Criteria:** As part of the system of internal controls, journal entries should be reviewed by someone other than the individual making the entry.

**Condition:** At the District, Shannon Daniels is primarily responsible for maintenance of the general ledger and journal entries. She prepares journal entries and enters them, without approval from or review by anyone else.

**Effect:** Errors could occur and not be detected in a timely manner. In addition, unauthorized entries could be made that may not be detected and corrected in a timely manner.

**Cause:** Journal entries are prepared and posted by Shannon and not reviewed by anyone at the District.

**Recommendation:** All journal entries should be reviewed and approved by the Executive Director or a transaction report of journal entries posted during the month could be included in the monthly financial packet that is provided to the Board for review and approval.

**Finding #12-02 Risk Assessment Processes**

**Criteria:** A risk assessment process should be part of management's and the board's policy that is addressed on an annual basis.

**Condition:** No process was noted during our interviews with management.

**Effect:** Changes in the business environment that the District operates in could increase business/management risks and steps may not be taken to address those risks in a timely manner.

**Cause:** No process was noted during our interviews with management.

**Recommendation:** A risk assessment process should be prepared and presented to the board for adoption.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
*For the Year Ended June 30, 2012 (continued)*

**II. Financial Statement Findings (continued)**

**Finding #12-03 Cash Management for Reimbursement Requests**

- Criteria:** Per the compliance supplement, program costs must be incurred and paid for by entity funds before a reimbursement is requested from the federal agency.
- Condition:** Reimbursement requests by the District included amounts that had not yet been paid by the District for retainage on construction projects.
- Effect:** Per the compliance supplement, if advances are requested, interest earned on the advances should be remitted to the agency. The effect is a possible liability to the federal agency.
- Cause:** Reimbursement requests included the entire amount of the project's pay estimate, including the portion of the costs incurred held as retainage by the contractor.
- Recommendation:** Retainage portion of the pay estimates need to be deducted from the requests for reimbursement until the retainage portion has been paid by the District.

**III. Federal Award Findings and Questioned Costs**

See #12-03 above.

**IV. Summary Schedule of Prior Audit Findings**

None

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
*For the Year Ended June 30, 2012 (continued)*

**V. Corrective Action Plan**

**Finding # 12-03**  
**Cash Management for**  
**Reimbursement**  
**Requests**

**Contact Person:** Shannon Daniels

**Response:** In the future, when the reimbursement requests are prepared, retainage payable will be deducted from the request. In addition, the overdrawn amount was netted against a subsequent reimbursement request.

**Estimated Date of Completion:** Immediately

**Finding # 12-01**  
**Journal Entry Process**

**Contact Person:** Shannon Daniels

**Response:** A journal entry report will be presented to the President for review and signature approval.

**Estimated Date of Completion:** Immediately

**Finding # 12-02**

**Risk Assessment**  
**Process**

**Contact Person:** Shannon Daniels

**Response:** The District will develop and implement a risk assessment process. The assessment will be reviewed annually by the Board Directors.

**Estimated Date of Completion:** January 2013

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF EXPENDITURE OF FEDERAL AWARDS**  
*June 30, 2012*

<u>Federal Grantor/ Pass Through Grantor/ Program Title</u>	<u>CFDA Number</u>	<u>Grantor Number</u>	<u>Federal Grant Expenditures</u>
<b>Federal Transit Administration</b>			
Federal Transit Capital Investment Grants			
<i>Intermodal Transit Terminal</i>	20.500	TX-04-0029-02	\$ 542,125
Federal Transit Formula Grants			
<i>Pedestrian/Transit Improvement Program</i>	20.507	TX-95-X005-01	5,169,890
<i>LCI Streetscape Improvements in Uptown - ARRA</i>	20.507	TX-66-X002-00	1,156,843
<b>Total Federal Transit Administration</b>			<u>6,868,858</u>
<b>Total Federal Awards</b>			<u>\$ 6,868,858</u>

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
*NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS*

**Note 1 - Summary of Significant Accounting Policies**

The District accounts for federal funding using the modified accrual method of accounting. This basis of accounting recognizes revenues in the accounting period in which they become susceptible to accrual, i.e. both measurable and available, and expenditures in the accounting period in which the liability is incurred, if measurable, except for compensated absences, claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources. Capital items for grant purposes are treated as expenses in the schedule of expenditures of federal awards.

Federal grant funds are considered to be earned to the extent of expenditures made under the provisions of the grant, and, accordingly, when such funds are received, they are recorded as deferred revenues until earned. Generally, unused balances are returned to the grantor at the close of specified project periods.

**Note 2 - Basis of Presentation**

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of the District under programs of the federal government for the year ended June 30, 2012. The information in this schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Government, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the financial position, changes in net assets or cash flows of the District.

**Note 3 - Reconciliation to Basic Financial Statements**

The Schedule of Expenditures of Federal Awards includes \$3,503,356 of expenditures in the Pedestrian/Transit Improvement Program that was incurred in the prior year. These expenditures were for projects that were approved by the Federal Agency in prior years but payment of those projects was contingent on available funds. The availability of federal funds did not become known until 2012.