

**HARRIS COUNTY
IMPROVEMENT DISTRICT NO. 1**

**ANNUAL FINANCIAL AND
COMPLIANCE REPORT**

**Year Ended June 30, 2019
with Independent Auditor's Report**

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
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INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund of Harris County Improvement District No. 1 (the "District") as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the District as of June 30, 2019, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 5 through 10 and the Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget to Actual on pages 33 through 34 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis, as required by Title 2 U.S. *Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic 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 basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated December 4, 2019, on our consideration of the District's internal control over financial reporting and on 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

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

Houston, Texas
December 4, 2019

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HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended June 30, 2019

As management of the Harris County Improvement District No. 1 (the "District"), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2019.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: (1) government-wide financial statements, (2) fund financial statements and (3) notes to the financial statements. This report also contains required supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The *Statement of Net Position* presents information on all of the District's assets and liabilities, and deferred outflows of resources with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator regarding the financial position of the District. Other factors that are not included in the financial statements, such as increased tax base in the District's boundaries, should be considered in evaluating the condition of the District's overall financial position.

The *Statement of Activities* presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of 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.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The District maintains three individual governmental funds. Information is presented separately in the *Governmental Fund Balance Sheet* and in the *Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances* for the General Fund, the Debt Service Fund, and the Capital Projects Fund, all of which are considered to be major funds.

Fund financial statements are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it may be useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the *Governmental Fund Balance Sheet* and the *Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances* provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Government-wide Financial Analysis

In the government-wide statements, net position is equal to the difference between assets and deferred outflows and liabilities. As previously noted, net position may serve over time as a useful indicator of a government's financial position. The District's net deficit at June 30, 2019, was \$2,636,667.

Net position is categorized based on the availability to provide financial resources for the District. Net position that is "Net Investment in capital assets" represent the District's capital assets, net of accumulated depreciation, less the outstanding balance of debt, excluding unspent bond proceeds, used to acquire those capital assets. Resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. "Restricted" net position represents amounts that are restricted for future debt service requirements. "Unrestricted" net position represents amounts available to meet the District's future obligations.

At year-end, the District had total assets of \$46,752,645 and deferred outflows of \$84,070. Of this amount, \$17,552,919 consisted of cash and cash equivalents, \$2,221,530 of investments, \$1,404,579 of construction in progress, and \$14,015,828 of other capital assets, net of depreciation. Total liabilities were \$44,200,048 as of year-end, which consisted of \$36,848,556 of long-term debt and accrued interest. The long-term debt consists of bonds issued to pay for construction projects within boundaries of the District. The other liabilities consists of accounts payable and other accrued liabilities. A comparative summary of the District's overall financial position, as of June 30, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Other assets	\$ 31,332,238	\$ 36,296,307
Capital assets, net of depreciation	<u>15,420,407</u>	<u>9,211,142</u>
Total Assets	<u>46,752,645</u>	<u>45,507,449</u>
Deferred Charge on Refunding	<u>84,070</u>	<u>104,206</u>
Total Deferred outflows	<u>84,070</u>	<u>104,206</u>
Other liabilities	4,993,908	7,297,340
Long-term liabilities	<u>39,206,140</u>	<u>31,859,916</u>
Total Liabilities	<u>44,200,048</u>	<u>39,157,256</u>
Net position:		
Net investment in capital assets	2,949,721	241,286
Restricted	3,335,684	3,246,852
Unrestricted	<u>(3,648,738)</u>	<u>2,966,261</u>
Total Net Position	<u>\$ 2,636,667</u>	<u>\$ 6,454,399</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The total net position of the District decreased by \$3,817,732. During the year ended June 30, 2019, net investment in capital assets increased by \$2,708,435 due to the additions related to Post Oak Boulevard Lighting projects, restricted net position increased by \$88,832, and unrestricted net position decreased by \$6,614,999 due to spending on capital projects and the issuance of the Series 2018 bonds. A comparative summary of the District's statement of activities for the past two years is as follows:

	<u>2019</u>	<u>2018</u>
Revenues		
Program revenue		
Charges for services	\$ 1,593,967	\$ 1,594,207
Capital Grants	23,547,925	24,110,736
General revenues		
Property taxes	8,800,102	8,584,757
Unrestricted investment earnings	296,756	182,153
Total Revenues	<u>34,238,750</u>	<u>34,471,853</u>
Expenses		
General and administrative	3,185,304	3,052,265
Traffic control	1,962,152	1,661,312
Maintenance and beautification	2,599,340	1,624,928
Planning and engineering	117,011	184,651
Marketing and communications	830,429	800,810
Interest on long-term debt	1,161,532	782,557
Economic development	49,528	36,723
Construction on behalf of the City of Houston	4,603,261	6,315,408
Transfers to other governments	23,547,925	24,110,736
Total Expenses	<u>38,056,482</u>	<u>38,569,390</u>
Increase (decrease) in net position	(3,817,732)	(4,097,537)
Net position - beginning	6,454,399	10,551,936
Net position - ending	<u>\$ 2,636,667</u>	<u>\$ 6,454,399</u>

Financial Analysis of the Government's Funds

The focus of the District's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the District's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$18,790,300, a decrease of \$1,967,082 in comparison with the prior year. This is due to spending on capital projects including the reconstruction of Hollyhurst and Post Oak Lane, pedestrian pylons for Post Oak Boulevard, and other lighting projects for Post Oak Boulevard.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The unassigned portion of fund balance is \$6,772,547 and is available for spending at the government's discretion. The remainder of fund balance is not available for spending because it has already been restricted for capital projects of \$8,286,137, debt service of \$3,629,744, or is classified as nonspendable.

The following is a summary of changes in fund balances for the prior two fiscal years:

	<u>2019</u>	<u>Increase (Decrease)</u>	<u>2018</u>	<u>Increase (Decrease)</u>	<u>2017</u>
General Fund	\$ 6,874,419	\$ (717,116)	\$ 7,591,535	\$ 679,929	\$ 6,911,606
Capital Projects Fund	8,286,137	(1,417,571)	9,703,708	(10,347,822)	20,051,530
Debt Service Fund	3,629,744	167,605	3,462,139	(198,449)	3,660,588
	<u>\$ 18,790,300</u>	<u>\$ (1,967,082)</u>	<u>\$ 20,757,382</u>	<u>\$ (9,866,342)</u>	<u>\$ 30,623,724</u>

The General Fund is the chief operating fund of the District. Fund balance in the General Fund decreased by \$717,116 during the current fiscal year. This decrease was due to operating expenditures exceeding ongoing revenues. As a measure of the General Fund's liquidity, it may be useful to compare unassigned fund balance to total fund expenditures. At the end of the current fiscal year, the unassigned portion of fund balance of the General Fund was \$6,772,547, while expenditures for the year were \$8,122,056.

The Debt Service Fund has a total fund balance of \$3,629,744, all of which is restricted for the payment of debt service. The increase in fund balance during the current year in the Debt Service Fund was \$167,605.

The Capital Projects Fund has total fund balance of \$8,286,137. The decrease in the fund balance during the current year in the Capital Projects Fund was \$1,417,571. The decrease is primarily related to capital project spending for Post Oak Boulevard, including lighting, and South Post Oak Lane.

General Fund Budgetary Highlights

There were no budget amendments during the year. The District did not anticipate an increase or decrease in fund balance, while the actual change resulted in a decrease to fund balance of \$717,116. Variances between budget and actual were due primarily to budget variances in spending related to maintenance and beautification projects.

Debt Administration

At June 30, 2019 and 2018, the District had total bonded debt outstanding as shown below:

<u>Series</u>	<u>2019</u>	<u>2018</u>
Series 2013	\$ 5,075,000	\$ 5,990,000
Series 2015	16,605,000	17,830,000
Series 2016	7,235,000	7,700,000
Series 2018	10,000,000	-
	<u>\$ 38,915,000</u>	<u>\$ 31,520,000</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Economic Factors and Next Year's Budgets and Rates

The District is a political subdivision of the State of Texas, created in 1987 by a special act of the 70th Texas Legislature. The District levies an ad valorem tax on real and personal property within its boundaries. The tax rate for tax year 2018 was \$0.14345 per \$100 of assessed value. The tax rate will remain the same for tax year 2019, with expected revenues of approximately \$6.0 million.

Office Space

Uptown Houston is one of the largest business districts outside a historic core in the United States. It is the 17th largest business district in the United States: comparable to Denver and Cleveland. With over 29 million square feet of total office space in its market area, Uptown accounts for over 13.7% of Houston MSA's total 'Class A' office space with over 20 million square feet. There are 127,000 office employees in the Uptown market area. At the end of the fourth quarter, 2018 class A office space was 84.75% leased similar to Houston's total Class A office market, also with occupancy at 83.8%.

The 2018 certified values for the office sector were up slightly from the previous year. The Uptown market area welcomed The Post Oak, Landry's 650,000 SF mixed-use tower with 140,000 SF of boutique office space. This new development is located close to Post Oak Boulevard and the 610 West Loop (located in the District). Hanover added almost 50,000 SF of office in their new residential tower which was completed in the fourth quarter of 2018 (also located in the TIRZ).

Currently, Zadok is constructing a 112,000 SF mixed-use development within TIRZ boundaries which includes 68,000 SF of office. Finally, in the Uptown market area, Park Place Tower, a 210,000 SF office tower, and 4411 San Felipe, an 80,000 SF officer tower, are under construction.

Retail

Uptown continues to be synonymous with high-end shopping and is known as a world-renowned center for retail. Ad valorem values for the retail sector for 2018 were up slightly from the previous year. Retail was 99% leased as of Q4 2018. This market maintained as The Galleria is now the fourth largest retail center in the United States. The Galleria Mall completed its reconstruction and renovation valued at \$250,000,000 at the corner of Westheimer and Sage. Totally redesigned, Saks Fifth Avenue is now open and their former space has been remodeled to house more high-end retail tenants. Uptown Park has begun an extensive modernization of their retail center bringing in both new retail stores as well as restaurants.

Hotel

Uptown now has 38 first quality hotels in the area, offering almost 8,300 rooms for guests. Landry's 36 story mixed-use development, "The Post Oak" is now open and recently received Houston's only AA Five-Diamond hotel rating. In the market area, American Liberty Hospitality is constructing a dual-branded Staybridge Suites/Holiday Inn Express with 319 rooms.

The area's RevPAR (revenues per available room) for 2018 Q4 is \$100.91 in comparison to the Houston Central Business District at \$124.77. The RevPAR for Houston City-wide is \$66.64. Uptown Houston also boasts one of the highest occupancy rates in the city at 68.6%, while the Houston City-wide occupancy rate was 63.2% at the end of the fourth quarter, 2018.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Residential

In 2018, Uptown market saw several residential projects delivered. Within the District boundaries, Hanover Boulevard Project (280 units) and The Post Oak (22 executive units) were delivered. In the Uptown market area, the Arabella Condominiums (99 units), The Wilshire condominiums (96 units), and the Overture Tanglewood apartments (192 units) were delivered. Currently under construction in the market area is the Reverie at River Hollow (304 apartment units) and the Gables Westcreek (302 apartment units). Within the District boundaries, the Aspire Post Oak apartments by Dinerstein (388 units) is under construction. Uptown Houston is one of the most prestigious and desirable areas to live.

The economic outlook is stable in Uptown. There continues to be new development in the area and property values are healthy year over year. While economic factors (property values, vacancy rates, future development, etc.) impact the size of debt issues, management takes a conservative approach to ensure that adequate resources are available to support the projects within the District.

Requests for Information

This financial report is designed to provide a general overview of the Harris County Improvement District #1's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to 1980 Post Oak Boulevard #1700, Houston, Texas 77056.

BASIC FINANCIAL STATEMENTS

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
STATEMENT OF NET POSITION - GOVERNMENTAL ACTIVITIES
June 30, 2019

Assets

Cash and cash equivalents	\$ 17,240,435
Restricted Cash	312,484
Investments	2,221,530
Property taxes receivable	173,931
Due from other governments	11,260,913
Other receivables	21,073
Prepaid items	101,872
Construction in progress	1,404,579
Other capital assets, net of depreciation	14,015,828
Total Assets	<u>46,752,645</u>

Deferred Outflows of Resources

Deferred Charge on Refunding	<u>84,070</u>
Total Deferred Outflows of Resources	<u>84,070</u>

Liabilities

Accounts payable and accrued expenses	1,903,396
Other payables	273,696
Due to other governments	2,471,178
Accrued interest	345,638
Noncurrent liabilities:	
Due in less than one year	2,703,222
Due in more than one year	36,502,918
Total Liabilities	<u>44,200,048</u>

Net Position

Net investment in capital assets	2,949,721
Restricted for debt service	3,335,684
Unrestricted	<u>(3,648,738)</u>
Total Net Position	<u>\$ 2,636,667</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
STATEMENT OF ACTIVITIES - GOVERNMENTAL ACTIVITIES
For the Year Ended June 30, 2019

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenue</u>		<u>Net (Expense) Revenue and Changes in Net Position</u>
		<u>Charges for Services</u>	<u>Capital Grants</u>	
General and administrative	\$ 3,185,304	\$ 1,540,000	\$ -	\$ (1,645,304)
Traffic Control	1,962,152	-	-	(1,962,152)
Maintenance and beautification	2,599,340	53,967	-	(2,545,373)
Planning and engineering	117,011	-	-	(117,011)
Marketing and communication	830,429	-	-	(830,429)
Interest on long-term debt and other charges	1,161,532	-	-	(1,161,532)
Economic development	49,528	-	-	(49,528)
Construction on behalf of the City of Houston	4,603,261	-	23,547,925	18,944,664
Transfers to other governments - Uptown Development Authority	23,547,925	-	-	(23,547,925)
Total activities	<u>\$ 38,056,482</u>	<u>\$ 1,593,967</u>	<u>\$ 23,547,925</u>	<u>(12,914,590)</u>

General revenues:	
Property taxes	8,800,102
Unrestricted investment earnings	296,756
Total general revenues and transfers	<u>9,096,858</u>
Change in net position	(3,817,732)
Net position - beginning	<u>6,454,399</u>
Net position - ending	<u>\$ 2,636,667</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**BALANCE SHEET - GOVERNMENTAL FUNDS**

June 30, 2019

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
Assets				
Cash and cash equivalents	\$ 6,731,110	\$ 7,549,307	\$ 2,960,018	\$ 17,240,435
Restricted Cash	312,484	-	-	312,484
Investments	-	2,221,530	-	2,221,530
Taxes receivable	122,353	-	51,578	173,931
Due from other funds	-	-	42,369	42,369
Due from other governments	265,660	2,643,072	8,352,181	11,260,913
Due from others	21,073	-	-	21,073
Prepaid items	101,872	-	-	101,872
Total Assets	<u>\$ 7,554,552</u>	<u>\$ 12,413,909</u>	<u>\$ 11,406,146</u>	<u>\$ 31,374,607</u>
Liabilities and Deferred Inflows				
Liabilities:				
Accounts payable	\$ 284,084	\$ 1,614,225	\$ 5,087	\$ 1,903,396
Due to other funds	-	42,369	-	42,369
Due to other governments	-	2,471,178	-	2,471,178
Other payables	273,696	-	-	273,696
Total Liabilities	<u>557,780</u>	<u>4,127,772</u>	<u>5,087</u>	<u>4,690,639</u>
Deferred Inflows of Resources				
Unavailable revenues - property taxes	122,353	-	51,578	173,931
Unavailable revenues - developer agreements	-	-	7,719,737	7,719,737
Total Deferred Inflows of Resources	<u>122,353</u>	<u>-</u>	<u>7,771,315</u>	<u>7,893,668</u>
Fund balances:				
Nonspendable	101,872	-	-	101,872
Restricted	-	8,286,137	3,629,744	11,915,881
Unassigned	6,772,547	-	-	6,772,547
Total Fund Balances	<u>6,874,419</u>	<u>8,286,137</u>	<u>3,629,744</u>	<u>18,790,300</u>
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	<u>\$ 7,554,552</u>	<u>\$ 12,413,909</u>	<u>\$ 11,406,146</u>	<u>\$ 31,374,607</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET POSITION
June 30, 2019

Total fund balance, governmental funds \$ 18,790,300

Amounts reported for governmental activities in the Statement of Net Position are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds.

Construction in progress	\$ 1,404,579	
Capital assets at historical cost	28,105,331	
Less accumulated depreciation	<u>(14,089,503)</u>	
Change due to capital assets		15,420,407

Property taxes receivable and related penalties and interest have been levied and are due, but are not available soon enough to pay current period expenditures and therefore, are deferred in the funds.

Property taxes receivable	113,181	
Penalty and interest receivable	<u>60,750</u>	
Change due to property taxes		173,931

Amounts due from project development agreements are due and, but are not available and therefore are deferred in the funds:

7,719,737

Some liabilities and deferred outflows are not due and payable in the current period and are not included in the fund financial statements, but are included in the Statement of Net Position. These are as follows:

Bonds payable	(38,915,000)	
Deferred charge on refunding	84,070	
Unamortized premiums	(250,607)	
Accrued interest	(345,638)	
Compensated absences	<u>(40,533)</u>	
Change due to long-term obligations		<u>(39,467,708)</u>

Net Position of Governmental Activities in the Statement of Net Position \$ 2,636,667

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
For the Year Ended June 30, 2019

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
Revenues				
Property taxes	\$ 5,751,769	\$ -	\$ 3,653,300	\$ 9,405,069
Intergovernmental	1,540,000	23,547,925	-	25,087,925
Investment earnings	59,204	222,587	14,965	296,756
Other Income	53,967	-	-	53,967
Total Revenues	<u>7,404,940</u>	<u>23,770,512</u>	<u>3,668,265</u>	<u>34,843,717</u>
Expenditures				
Current:				
Planning and engineering	117,011	-	-	117,011
Traffic control	1,361,689	-	-	1,361,689
Maintenance and beautification	2,599,340	-	-	2,599,340
General and administrative	3,174,059	-	-	3,174,059
Marketing and communications	820,429	-	-	820,429
Economic development	49,528	-	-	49,528
Debt Service:				
Principal	-	-	2,605,000	2,605,000
Interest and other charges	-	217,169	895,660	1,112,829
Capital Outlay	-	11,422,989	-	11,422,989
Transfers to other governments -				
Uptown Development Authority	-	23,547,925	-	23,547,925
Total Expenditures	<u>8,122,056</u>	<u>35,188,083</u>	<u>3,500,660</u>	<u>46,810,799</u>
Excess (deficiency) of Revenues over Expenditures	<u>(717,116)</u>	<u>(11,417,571)</u>	<u>167,605</u>	<u>(11,967,082)</u>
Other Financing Sources/(Uses):				
Proceeds from long-term debt	-	10,000,000	-	10,000,000
Total Other Financing Sources/(Uses)	<u>-</u>	<u>10,000,000</u>	<u>-</u>	<u>10,000,000</u>
Net change in Fund Balances	(717,116)	(1,417,571)	167,605	(1,967,082)
Fund Balances - beginning of year	<u>7,591,535</u>	<u>9,703,708</u>	<u>3,462,139</u>	<u>20,757,382</u>
Fund Balances - end of year	<u>\$ 6,874,419</u>	<u>\$ 8,286,137</u>	<u>\$ 3,629,744</u>	<u>\$ 18,790,300</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2019

Net change in fund balances - total governmental funds: \$ (1,967,082)

Amounts reported for Governmental Activities in the Statement of Activities are different because:

Governmental funds do not report revenues that are not available to pay current obligations. In contrast, such revenues are reported in the Statement of Activities when earned.

Property taxes and related penalties and interest	\$ 27,477	
Project development agreement revenue	(632,444)	
		(604,967)

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the costs of those assets is allocated over their estimated useful lives and reported as depreciation expense for the period.

Capital outlay expenditures	\$ 6,819,728	
Depreciation expense	(600,463)	
Gain/(loss) on disposal of capital assets	(10,000)	
Change due to capital assets		6,209,265

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of principal uses current financial resources. However, at the government-wide level these transactions have the effect of increasing or decreasing long-term liabilities.

Principal payment of debt	2,605,000	
Proceeds from issuance of debt	(10,000,000)	
Premium is amortized over the life of the bond	60,021	
Deferred charge on refunding is amortized over the life of the bond	(20,136)	
		(7,355,115)

Some expenses reported in the statement of activities do not require the use of current financial resources and are not reported as expenditures in governmental funds. These are as follows:

Change in compensated absences	(11,245)	
Change in interest payable	(88,588)	
		(99,833)

Change in net position of governmental activities \$ (3,817,732)

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HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS

June 30, 2019

A. Summary of Significant Accounting Policies

The financial statements of Harris County Improvement District No. 1 (“the District”) have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Government Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and reporting principles. The following is a summary of the most significant policies.

Creation

Harris County Improvement District No. 1 (the “District”) was organized, created, and established pursuant to an act of the 70th Texas State Legislature, effective under the terms and provisions of Article III, Section 52 and Article XVI, Section 59 of the Texas Constitution. The Board of Directors held its organizational meeting on July 18, 1987. The first bonds were sold on June 23, 1993. See Note F for additional information regarding significant legal provisions contained in the legislative act creating the District.

The District's primary activities include managing and financing improvement projects and/or services benefiting the District. These activities include maintenance and beautification of the area, traffic control and transportation projects, special events for the holiday seasons, general planning and engineering, area marketing, major capital improvements and general and administrative services.

Reporting Entity

The District is a political subdivision of the State of Texas, governed by an appointed board, and is considered a primary government. The GASB has established the criteria for determining whether or not an entity is a primary government or a component unit of a primary government. The primary criteria are that it has a separately elected governing body; it is legally separate; and it is fiscally independent of other state and local governments. Under these criteria, the District is considered a primary government and is not a component unit of any other government. Additionally, no other entities meet the criteria for inclusion in the District’s financial statements as component units.

Government-wide and Fund Financial Statements

Government-wide financial statements display information about the District as a whole. These statements focus on the sustainability of the District as an entity and the change in aggregate financial position resulting from activities of the fiscal period. Interfund activity, if any, has been removed from these statements. The government wide statements consist of the *Statement of Net Position* and the *Statement of Activities*.

The *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes: (1) charges to customers or applicants, who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular segment. Taxes and other items not properly included among program revenues are reported as general revenues.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

A. Summary of Significant Accounting Policies (continued)

Government-wide and Fund Financial Statements

Fund financial statements display information at the individual fund level. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for a specific purpose. Each fund is considered to be a separate accounting entity. These fund financial statements are the *Governmental Funds- Balance Sheet* and the *Governmental Funds - Statement of Revenues, Expenditures and Changes in Fund Balances*

The District reports the following major governmental funds:

The *General Fund* is used to account for administrative operations of the District. The principal source of revenue is property taxes. Expenditures include all costs associated with the daily operations of the District.

The *Debt Service Fund* is used to account for the payment of interest and principal on all general long-term debt of the District. The primary source of revenue is provided by contract tax increment revenue.

The *Capital Projects Fund* is used to account for the expenditure of bond proceeds used in the construction of authorized improvement projects.

Measurement Focus and Basis of Accounting

The Government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available if they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal period; property taxes are recognized when collected. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Deposits and Investments

Investments for the District are reported at fair value. The depository cash balances were covered by FDIC insurance and by collateral held by the District's agent in the District's name. The District categorizes fair value measurements of its investments based on the hierarchy established by generally accepted accounting principles. The fair value hierarchy, which has three levels, is based on the valuation inputs used to measure an asset's fair value: Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; level 3 inputs are significant unobservable inputs.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

A. Summary of Significant Accounting Policies (continued)

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. At June 30, 2019, an allowance for uncollectible property tax accounts was not considered necessary.

Prepaid Items

Certain payments made by the District reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.

Capital Assets

Capital assets are reported in the government-wide financial statements. The District defines capital assets as assets with an initial, individual cost of \$5,000 or more and an estimated useful life in excess of one year. Capital assets are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at the estimated fair value at the date of donation. Assets are depreciated over their remaining useful lives using the straight-line method.

Asset	Estimated Useful Lives
Machinery and Equipment	10 - 20 years

Fund Balance / Restricted Assets

The District records reservations for all or portions of governmental fund balances which are legally segregated for specific future use or which do not represent available spendable resources and therefore not available for appropriation. Unassigned fund balance indicates the portion of fund balance which is available for appropriation in future periods. The restricted fund balances for governmental funds represent the amount that has been identified for specific purposes.

The District applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

The following fund balance classifications describe the relative strength of the spending constraints:

Nonspendable fund balance – amounts that are not in spendable form or are required to be maintained intact. As such, the inventory and prepaid items have been properly classified in the Governmental Funds Balance Sheet.

Restricted fund balance – Amounts that can be spent only for specific purposes because of local, state or federal laws, or externally imposed conditions by grantors or creditors.

Committed fund balance – amounts constrained to specific purposes by the District itself, using its highest level of decision-making authority (i.e. the Board of Directors). To be reported as committed, amounts cannot be used for any other purposes unless the District takes the same highest level of action to remove or change the constraint.

Assigned fund balance – amounts the District intends to use for a specific purpose. Intent can be expressed by the Authority or by an official or body to which the Board of Directors delegates the authority. Funds maybe be assigned by the District’s president or by the Board of Directors for specific purposes through the budget process or agenda items.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

A. Summary of Significant Accounting Policies (continued)

Fund Balance / Restricted Assets (continued)

Unassigned fund balance – amounts that are available for any purpose. Positive amounts are reported only in the general fund.

The District establishes (and modifies or rescinds) fund balance commitments by passage of a resolution. When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the District considers restricted funds to have been spent first. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the District considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds. The District has nonspendable, restricted and unassigned fund balances as of June 30, 2019.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/ expenditure) until then. The District only has one item that qualifies for reporting in this category. It is the deferred charge on refunding reported in the government-wide statement of net position. A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt. At year-end, the District had a deferred outflow of \$84,070.

In addition to liabilities, the governmental funds balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of fund balance that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. The District has unavailable revenues for property taxes including penalty and interest of \$173,931, and developer agreements of \$7,719,737 that qualify for reporting in this category, which arise only under a modified accrual basis of accounting.

Interfund Activity

During the course of operations, transactions occur between individual funds. This can include internal transfers, payables and receivables. This activity is combined as internal balances and is eliminated in both the government-wide and fund financial statements.

Compensated Absences

The District's employees earn vacation leave, which may either be taken or accumulated, up to certain amounts, until paid upon termination or retirement. The amounts are recorded as a liability in the *Statement of Net position*.

Use of Estimates

The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

A. Summary of Significant Accounting Policies (continued)

New Accounting Standard

In the current fiscal year, the District implemented GASB Statement No. 88, Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements, to improve consistency in the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements, and to provide financial statement users with additional essential information about debt

B. Deposits and Investments

The cash deposits were comprised of demand accounts and were entirely covered by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 or by pledged collateral held by the District's agent banks in the District's name as of June 30, 2019.

These District's money market mutual funds and certificates of deposit are reported at fair value using Level 1 inputs and the U.S. Treasury Notes are reported at fair value using Level 2 inputs. As of June 30, 2019, the District's investments were comprised of the following:

	<u>Amount</u>	<u>Weighted Average Maturity</u>	<u>Rating</u>
Money Markey Mutual Funds	\$ 1,221,686	39	AAAm
U.S. Treasury Notes	999,844	-	AAA/AA+
Certificates of Deposit	1,500,000	80	N/A
	<u>\$ 3,721,530</u>	45	

Authorized Investments

The District is authorized by the Public Funds Investment Act (Chapter 2256, Texas Government Code) to invest in the following: (1) obligations of the United States or its agencies and instrumentalities, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) certain collateralized mortgage obligations, (4) other obligations, which are unconditionally guaranteed or insured by the State of Texas or the United States or its agencies or instrumentalities, (5) certain A rated or higher obligations of states and political subdivisions of any state, (6) bonds issued, assumed or guaranteed by the State of Israel, (7) insured or collateralized certificates of deposit, (8) certain fully collateralized repurchase agreements, (9) bankers' acceptances with limitations, (10) commercial paper rated A-1 or P-1 or higher and a maturity of 270 days or less, (11) no-load money market mutual funds and no-load mutual funds, with limitations, (12) certain guaranteed investment contracts, (13) certain qualified governmental investment pools and (14) a qualified securities lending program.

The District has adopted a written investment policy to establish the principles by which the District's investment program should be managed. This policy further restricts the types of investments in which the District may invest.

Investment Credit and Interest Rate Risk

Investment credit risk is the risk that the investor may not recover the value of an investment from the issuer, while interest rate risk is the risk that the value of an investment will be adversely affected by changes in interest rates. The Authority's investment policies do not address investment credit and interest rate risk beyond the rating and maturity restrictions established by state statutes.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

B. Deposits and Investments (continued)

Restricted Cash

As discussed in Note I, the District has entered into an agreement for deferred compensation for certain employees, the amount in the plan's account is restricted for additional compensation to certain employees after their retirement, or a death benefit to the employees' designated beneficiaries after their deaths.

C. Capital Assets

A summary of changes in capital assets, for the year ended June 30, 2019, follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>(Retirements)</u>	<u>Transfers</u>	<u>Ending Balances</u>
Capital assets, not being depreciated					
Construction in progress	\$ 4,006,003	\$ 4,572,656	\$ -	\$(7,174,080)	\$ 1,404,579
Total Capital assets, not being depreciated	<u>4,006,003</u>	<u>4,572,656</u>	<u>-</u>	<u>(7,174,080)</u>	<u>1,404,579</u>
Capital assets, being depreciated:					
Machinery and equipment	19,594,879	-	(910,700)	7,174,080	28,105,331
Less accumulated depreciation	(14,389,740)	-	900,700	-	(14,089,503)
Total Capital assets, net of depreciation	<u>5,205,139</u>	<u>-</u>	<u>(10,000)</u>	<u>7,174,080</u>	<u>14,015,828</u>
Governmental Capital Assets	<u>\$ 9,211,142</u>	<u>\$ 4,572,656</u>	<u>\$ (10,000)</u>	<u>\$ -</u>	<u>\$ 15,420,407</u>

Depreciation was charged to the Traffic Control function of the District in the amount of \$600,463

D. Long-Term Liabilities

During the year, the District's long-term liabilities changed as outlined below:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable from public placements	\$ 5,990,000	\$ -	\$ (915,000)	\$ 5,075,000	\$ 950,000
Bonds payable from private placements	25,530,000	10,000,000	(1,690,000)	33,840,000	1,725,000
Unamortized premiums	310,628	-	(60,021)	250,607	-
Compensated absences	29,288	132,180	(120,935)	40,533	28,222
	<u>\$ 31,859,916</u>	<u>\$ 10,132,180</u>	<u>\$ (2,785,956)</u>	<u>\$ 39,206,140</u>	<u>\$ 2,703,222</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

D. Long-Term Liabilities (continued)

Bonds payable as of June 30, 2019 consists of the following:

<u>Series</u>	<u>Amount Outstanding</u>	<u>Original Issue</u>
Public Placement		
Unlimited Tax Refunding Bonds, Series 2013	\$ 5,075,000	\$ 9,300,000
Private Placement		
Unlimited Tax Bonds, Series 2015	\$ 16,605,000	\$ 20,365,000
Unlimited Tax Bonds, Series 2016	7,235,000	8,150,000
Unlimited Tax Bonds, Series 2018	10,000,000	10,000,000
Total Private Placement	<u>\$ 33,840,000</u>	

On October 25, 2018, the District issued \$10,000,000 Tax Increment Contract Revenue Bonds, Series 2018. The bonds have an interest rate of 3.39 percent. The bonds will be used (1) for the stimulation and development of transportation and (2) to pay the costs associated with the issuance of the Bonds. The Bonds mature June 30, 2033.

During the fiscal year ended June 30, 2013, the District issued 2013 Refunding Bonds, refunding a portion of the 1999 and the 2004 bond issues. The reacquisition price exceeded the net carrying amount of the old debt by \$204,886. This resulting deferred outflow is amortized over the life of the Bond.

	<u>Previous Balance</u>	<u>Current Year</u>	<u>Year End Balance</u>
Deferred loss on refunding	\$ 104,206	\$ (20,136)	\$ 84,070
	<u>\$ 104,206</u>	<u>\$ (20,136)</u>	<u>\$ 84,070</u>

Payment of principal and interest on the bonds is to be provided from tax levies on properties within the District. As the bonds are unlimited tax bonds, no other funds of the District have been pledged for debt service requirements. Investment income realized by the Debt Service Fund, from investment of excess funds, will be used to pay outstanding bond principal and interest. The District is in compliance with all significant requirements and restrictions contained in its bond resolution.

Annual debt service requirements to retire public placement bonds are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2020	\$ 950,000	\$ 148,700	\$ 1,098,700
2021	990,000	119,600	1,109,600
2022	1,020,000	89,450	1,109,450
2023	1,045,000	58,475	1,103,475
2024	1,070,000	21,400	1,091,400
	<u>\$ 5,075,000</u>	<u>\$ 437,625</u>	<u>\$ 5,512,625</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

D. Long-Term Liabilities (continued)

Annual debt service requirements to retire private placement bonds are as follows:

Year Ending June 30,	Principal	Interest	Total
2020	\$ 1,725,000	\$ 977,178	\$ 2,702,178
2021	1,760,000	929,485	2,689,485
2022	1,800,000	880,772	2,680,772
2023	1,810,000	831,298	2,641,298
2024	1,940,000	779,548	2,719,548
2025	2,515,000	716,071	3,231,071
2026	2,585,000	641,954	3,226,954
2027	2,665,000	565,588	3,230,588
2028	2,740,000	486,908	3,226,908
2029	2,820,000	405,915	3,225,915
2030	2,900,000	322,546	3,222,546
2031	2,985,000	236,717	3,221,717
2032	3,070,000	141,215	3,211,215
2033	2,525,000	42,799	2,567,799
	<u>\$ 33,840,000</u>	<u>\$7,957,994</u>	<u>\$ 41,797,994</u>

A summary of District Bonds authorized, but unissued at June 30, 2019 follows:

Purpose	Date Authorized	Amount Authorized	Amount Unissued
Stimulation and development of transportation	05/30/92	\$ 75,000,000	\$ 21,410,000
Conservation and preservation of natural resources	05/30/92	25,000,000	21,995,000
Improvement projects payable from assessments	05/30/92	25,000,000	25,000,000
Improvement projects for economic diversification	11/20/93	25,000,000	25,000,000
		<u>\$ 150,000,000</u>	<u>\$ 93,405,000</u>

E. Property Taxes

On May 30, 1992, the voters of the District authorized the District's Board of Directors to levy taxes annually for use in financing general operations (maintenance tax) limited to \$0.25 per \$100 of assessed property valuation. The Harris County Appraisal District determines all property valuations and exempt status, if any. The District's bond resolution requires that property taxes be levied for use in paying interest and principal on long-term debt and for use in paying costs incurred in assessment and collection of these taxes. Taxes levied for debt service and related costs are without limitation as to rate or amount.

The District has contracted with the Harris County Tax Assessor/Collector for its tax levy and collection functions. A tax lien attaches to properties within the District on January 1 of each year when property valuations for use in levying taxes are established. Taxes levied are generally billed in October and are due upon receipt of the tax bill. Penalty and interest are charged if taxes are not paid by January 31. There is an additional 15% penalty charged on accounts delinquent after July 1, which generally is payable to the District's delinquent tax attorney.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE FINANCIAL STATEMENTS (continued)

E. Property Taxes (continued)

Property taxes are collected based on rates adopted in the year of the levy. The District’s fiscal year ended June 30, 2019, was financed through the 2018 tax levy. The District levied property taxes of per \$100 of assessed value, of which \$0.094450 was allocated to maintenance and operations and \$0.049 was allocated to debt service. The resulting tax levy was \$9,191,120 on the adjusted taxable value of \$6,407,256,884.

Taxes receivable, at June 30, 2019, consisted of the following:

Current year taxes receivable	\$	46,129
Delinquent taxes receivable		<u>67,052</u>
		113,181
Penalty and interest receivable		<u>60,750</u>
Total property taxes receivable	\$	<u><u>173,931</u></u>

F. Significant Legal Provisions of Legislative Act Creating District

As discussed in Note A above, the District has been established pursuant to an act of the Texas State Legislature. Significant legal provisions of this act are summarized below.

District Boundaries

The Act provides specifically for boundaries of the District, which includes the Uptown Houston area. The Uptown Houston area is also known as the Galleria-Post Oak area in Houston, Texas. The District may annex additional land area in accordance with Chapter 54 of the Texas Water Code. On May 22, 2013, Harris County Improvement District No. 1 adopted an Order Adding Land (responding to a petition of the landowners) adding 33.99 acres of land (located in the vicinity of the intersection of US 59 and IH 610) to the District.

Texas Commission on Environmental Quality Involvement

The Act provides that the Texas Commission on Environmental Quality is to appoint District Directors. The Directors are to serve staggered four-year terms. Additionally, the Texas Commission on Environmental Quality must approve the issuance of any bonded indebtedness for the purposes of providing water, sewer or drainage facilities within the District. No other District activities are subject to the jurisdiction of the Texas Commission on Environmental Quality.

General and Specific Powers of the District

The Act provides general powers to the District subject to general laws and regulations of the state applicable to conservation and reclamation districts created under Article XVI, Section 59 of the Texas Constitution and road districts and road utility districts created pursuant to Article III, Section 52, of the Texas Constitution, including those conferred by Chapter 54 of the Water Code and Chapter 13, Acts of the 68th legislature, 2nd Called Session, 1984 (Article 6674r-1, Vernon’s Texas Civil Statutes).

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

F. Significant Legal Provisions of Legislative Act Creating District (continued)

General and Specific Powers of the District (continued)

Additional specific powers and duties are provided for in the act, which include the financing of improvement projects and/or services for the benefit of the District. Specific types of improvement projects are provided for in the act and include the acquisition of land in connection with the improvements. Eminent domain powers are specifically prohibited by the act. Improvement projects and/or services may be financed in whole or in part by the levy and collection of special assessments or property taxes on property in the area. The act also provides that maintenance taxes may be levied after voter approval.

The Act provides for the method by which the District must petition, provide notice and hold public hearings prior to the financing of the improvement projects and/or services.

The Act also provides for the issuance of voter-approved bonded indebtedness to finance improvement projects and/or services. Specific guidelines in the act provide for the repayment of bonds, which might be issued, as well as the use of bond proceeds, available security that can be pledged in issuing the bonds and refunding capabilities for outstanding bonds.

Director Bonds

The Act requires that each Director appointed execute a bond for \$10,000 payable to the District and conditioned on faithful performance of his or her duties. All bonds of the Directors shall be approved by the Board.

G. Operating Agreement - Uptown Development Authority

The District has entered into an operating agreement with Uptown Development Authority (the "Authority"). The Authority is a component unit of the City of Houston formed to carry out improvements in the Uptown Houston area. The governing boards of both the District and the Authority have common members. It is the intent of both governing boards to maintain separately controlled operating entities. The agreement calls for the District to perform services as and when requested by the Authority Board. The services may consist of general administrative support, project management and development, consultant management, and other services as may be deemed necessary. The District is the recipient of federal grants for pedestrian and intersection improvements within the District. Additionally, the Authority has an approved capital improvement plan which includes pedestrian and intersection improvements. These two entities work with each other with the Authority providing the local match and the implementation of the project while the District will provide the grant funds (see Note N). Financial information regarding the Authority can be obtained from Uptown Development Authority, 1980 Post Oak Boulevard #1700, Houston, Texas 77056.

Financing Agreement - Uptown Development Authority

The District has a Finance Agreement with the Uptown Development Authority (The UDA) in which the Authority could borrow up to \$3.5 million, which is to be repaid by the Authority's fiscal year-end (June 30, 2019). While this agreement is still in place, the Authority did not make use of requesting funds from the District. This agreement is reviewed and approved annually by both Boards of Directors.

H. Pension Plan

For the benefit of its employees, the District provides discretionary contributions to a simplified employee pension plan, meeting the requirements of Internal Revenue Code Section 408(k). For the year ended June 30, 2019, the District contributed \$154,375 to the plan.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

I. Deferred Compensation

During the fiscal year ended June 30, 2019, the district entered into a Retirement Plan governed by the provisions of Section 457(f) of the Internal Revenue Code of 1986, as amended. Each year, the District's Board determines the contribution to be made for additional compensation to certain eligible employees after their retirement, or a death benefit to the employees' designated beneficiaries after their deaths. For the year ended June 30, 2019, the District contributed \$99,586 to the plan and the amount in the Retirement Plan as of June 30, 2019 is \$312,484.

J. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and personal injuries. The risk of loss is covered by commercial insurance. There have been no significant reductions in insurance coverage. Settlement amounts have not exceeded insurance coverage for current year or the three prior years.

K. Tax Increment Reinvestment Zone

During the current and prior years, the District incurred certain planning expenditures related to the Tax Increment Reinvestment Zone No. 16 of the City of Houston (TIRZ). The TIRZ is located on property generally within the District's service area. During the year ended June 30, 2019, the District received \$1,540,000 from the TIRZ for reimbursement of administration costs, project management costs and traffic and mobility costs.

L. Federal Grants

The District is a recipient of a federal grant for pedestrian and intersection improvements: Congestion Mitigation and Air Quality (CMAQ) 80/20 Grant and a Congressional appropriated Discretionary Grant. In accordance with the operating agreement with the Uptown Development Authority (UDA); the grant funds are used to fund the UDA's capital improvement plan. The UDA expends all funds for purposes of the grant, including a 20% local matching requirement under the CMAQ grant terms. All grant revenues are recognized by the District based on the UDA spending and are then paid to the UDA as a reimbursement for grant related spending.

A summary of grant activity through June 30, 2019, is shown below along with similar information for the total grant.

<u>Funding Source</u>	<u>Cumulative Amounts</u>	
	<u>Actual through June 30, 2019</u>	<u>Total Grant Awarded</u>
Congestion Mitigation Air Quality Federal (CMAQ) Grant (80%)	\$ 67,375,813	\$ 88,767,462
Congressional Appropriated Discretionary Grant	2,464,244	2,665,864
	<u>\$ 69,840,057</u>	<u>\$ 91,433,326</u>

The CMAQ and the Discretionary Grant both require a 20 percent match, which is made by the UDA. For the cumulative period ending June 30, 2019, the UDA provided the required local match of \$4,709,585.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

M. Project Development Agreement

The District has entered into a financing agreement with the Uptown Development Authority for advancing funds to the Authority for the purpose of financing the construction of public works and improvements (Hollyhurst and Post Oak Lane). Under the agreement, the District will fund the construction of these certain facilities and improvements within the Zone. These facilities and improvements will be conveyed to the City or other governmental entity upon completion of construction and inspection and acceptance by the City or other governmental entity. The District will be reimbursed from available tax increment attributable to the Hollyhurst and Post Oak Lane projects. The Authority agrees to repay 100% of all funds advanced including cost of issuance and interest on bonds issued to fund the projects. The District issued \$8,150,000 in bonds for this purpose. Amounts reported as due from other governments for this purpose as of June 30, 2019 is \$8,352,181 and \$7,719,737 is unavailable revenue as the payments will not be received within 60 days of year-end.

N. Related Party Transactions

Mizington Incorporated

Harris County Improvement District #1 (HCID #1) has a service agreement with Mizington Incorporated for professional services. The Mizington employees are former HCID #1 employees. Mizington was created to provide employees with the option to contribute to social security as HCID #1 employees do not.

Uptown Development Authority

The District has entered into an operating agreement with Uptown Development Authority (the "Authority"). It is the intent of both governing boards to maintain separately controlled operating entities. There is one member of the District board that also serves on the Authority board. The agreement calls for the District to perform services as and when requested by the Authority Board. The services may consist of general administrative support, project management and development, consultant management, and other services as may be deemed necessary.

The Authority has an approved capital improvement plan which includes the reconstruction of Post Oak Boulevard. This Authority project requires the purchase of rights-of-way along Post Oak Boulevard. While the Authority is the purchaser, there are some parcels along the Boulevard that are owned and/or affiliated by/with members of the District board.

REQUIRED SUPPLEMENTARY INFORMATION

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HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - BUDGET TO ACTUAL
June 30, 2019

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive/ (Negative)
Revenues				
Property taxes	\$ 5,999,903	\$ 5,999,903	\$ 5,751,769	\$ (248,134)
Intergovernmental	1,540,000	1,540,000	1,540,000	-
Shelter program (Metro)	33,263	33,263	-	(33,263)
Investment earnings	16,394	16,394	59,204	42,810
Grant proceeds	23,235,000	23,235,000	23,547,925	312,925
Miscellaneous	-	-	53,967	53,967
Total Revenues	30,824,560	30,824,560	30,952,865	128,305
Expenditures				
Current:				
Planning and engineering	150,000	150,000	117,011	32,989
Traffic control	1,365,970	1,365,970	1,361,689	4,281
Maintenance and beautification	1,774,699	1,774,699	2,599,340	(824,641)
General and administrative	3,203,949	3,203,949	3,174,059	29,890
Marketing and communications	750,000	750,000	820,429	(70,429)
Economic development	71,900	71,900	49,528	22,372
Transfer of Grants to UDA	23,235,000	23,235,000	23,547,925	(312,925)
Total Expenditures	30,551,518	30,551,518	31,669,981	(1,118,463)
Excess (deficiency) of revenues over expenditures	273,042	273,042	(717,116)	990,158
Other Financing Sources (Uses)				
Transfers out	(273,042)	(273,042)	-	(273,042)
Total Other Financing Sources (uses)	(273,042)	(273,042)	-	(273,042)
Net change in fund balance	-	-	(717,116)	(717,116)
Fund balance - beginning of year	7,591,535	7,591,535	7,591,535	-
Fund balance - end of year	\$ 7,591,535	\$ 7,591,535	\$ 6,874,419	\$ (717,116)

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

June 30, 2019

Budgets and Budgetary Accounting

A non-appropriated budget is adopted for the General Fund by the District's Board of Directors. The budget is considered a planning tool and does not constitute legal spending limit authority. The budget is prepared using the same method of accounting as for the financial reporting except that the General Fund budget includes federal grant revenues and the related transfers. For financial reporting purposes, the federal grant revenues (included in HGAC grants in the preceding schedule) and the related transfers to UDA are reported in the Capital Projects Fund as an intergovernmental revenue and as an expenditure, respectively.

Prior to July 1, 2018, the District adopted its annual budget, or Original Budget, any amendments to the budget are made throughout the year but prior to June 30, 2019 to present a Final Budget as of June 30, 2019. There were no amendments to the budget during the fiscal year.

Budget Overages

The Schedule of Revenues, Expenditures and Changes in Fund Balances – Budget to Actual presents budget overages in certain expenditures. Maintenance and beautification expenditures exceeded the budget by \$824,641 due to more than anticipated expenditures for holiday lighting projects for all District streets excluding Post Oak Boulevard. Marketing and Communications expenditures exceeded the budget by \$70,429 due to the events and additional projects conceived and implemented after the budget year began to highlight/promote and support Uptown. Transfers of Grants to UDA exceeded the budget by \$312,925 due to more than expected capital projects conducted at UDA related to the Post Oak Boulevard, Transit Center, and other capital projects. Overall the District exceeded its operating expenditures budget by \$1,118,463.

**INDEPENDENT AUDITOR'S 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, 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, 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, 2019, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated December 4, 2019.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

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. *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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Whitley Penn LLP

Houston, Texas
December 4, 2019

INDEPENDENT AUDITOR’S REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE *UNIFORM GUIDANCE*

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

Report on Compliance for Each Major Federal Program

We have audited Harris County Improvement District No. 1’s (the “District”) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the District’s major federal program for the year ended June 30, 2019. The District’s major federal program is identified in the summary of auditor’s results section of the accompanying schedule of findings and questioned costs.

Management’s Responsibility

Management is responsible for compliance with the federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor’s Responsibility

Our responsibility is to express an opinion on compliance for the District’s major federal program based on our audit of the types of compliance requirements referred to above. 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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance 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 on compliance for the major federal program. However, our audit does not provide a legal determination of the District’s compliance.

Opinion on Each Major Federal Program

In our opinion, Harris County Improvement District No. 1 complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2019.

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

Report on Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with Uniform Guidance, 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. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



Houston, Texas
December 4, 2019

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended June 30, 2019

I. Summary of Auditors' Results

Financial Statements

Type of auditors' report issued	Unmodified
Internal control over financial reporting:	
Material weakness (es) identified?	No
Significant deficiency (ies) identified that are not considered to be material weaknesses?	None reported
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:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	None

Identification of Major Programs:

Name of Federal Program	CFDA Number
Federal Transit Cluster:	
Federal Transit – Formula Grants	20.507
Dollar Threshold Considered Between Type A and Type B Federal Programs	\$750,000
Auditee qualified as low-risk auditee?	Yes

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended June 30, 2019

II. Financial Statement Findings

No current year findings.

III. Federal Award Findings and Questioned Costs

No current year findings.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended June 30, 2019

<u>Federal Grantor/ Pass Through Grantor/ Program Title</u>	<u>CFDA Number</u>	<u>Grantor Number</u>	<u>Federal Grant Expenditures</u>
Department of Transportation			
Direct:			
<u>Federal Transit Cluster:</u>			
<i>Federal Transit Formula Grants:</i>			
<i>Post Oak Dedicated Bus Lanes/Trust Ctr</i>	20.507	TX-95-Y005-00	\$ 16,926,723
<i>Bellaire Uptown Transit Center</i>	20.507	TX-95-Y005-00	<u>6,621,202</u>
Total Federal Transit Cluster			<u>23,547,925</u>
Total Department of Transportation			<u>23,547,925</u>
Total Federal Awards			<u>\$ 23,547,925</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended June 30, 2019

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 expenditures 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 unearned revenues until earned. Generally, unused balances are returned to the grantor at the close of specified project periods. The District has elected not to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance

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, 2019. The information in this schedule is presented in accordance with the requirements of the Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). 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 position or cash flows of the District.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

For the Year Ended June 30, 2019

Federal regulations, Title 2 U.S. Code of Federal Regulations Section 200.511 states, "The auditee is responsible for follow-up and corrective action on all audit findings. As part of this responsibility, the auditee must prepare a summary schedule of prior audit findings." The summary schedule of prior audit findings must report the status of the following:

- All audit findings included in the prior audit's schedule of findings and questioned costs and
- All audit findings reported in the prior audit's summary schedule of prior audit findings except audit findings listed as corrected.

I. Prior Audit Findings

None Noted.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

CORRECTIVE ACTION PLAN

For the Year Ended June 30, 2019

Federal regulations, Title 2 U.S. Code of Federal Regulations §200.511 states, “At the completion of the audit, the auditee must prepare, in a document separate from the auditor's findings described in §200.516 Audit findings, a corrective action plan to address each audit finding included in the current year auditor's reports.”

I. Corrective Action Plan

Not Applicable