

**HARRIS COUNTY  
IMPROVEMENT DISTRICT NO. 1**

**ANNUAL FINANCIAL AND  
COMPLIANCE REPORT**

**Year Ended June 30, 2018  
with Independent Auditor's Report**



# HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

## FINANCIAL REPORT

Year Ended June 30, 2018

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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, 2018, 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, 2018, 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 7 through 12 and the Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget to Actual on pages 35 through 36 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.

Board of Directors  
Harris County Improvement District No. 1

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 12, 2018, 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 12, 2018

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## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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# HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended June 30, 2018

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, 2018.

### 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, the difference between assets and deferred outflows and liabilities is called net position. As previously noted, net position may serve over time as a useful indicator of a government’s financial position. The District’s net position at June 30, 2018, was \$6,454,399.

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 \$45,507,449 and deferred outflows of \$104,206. Of this amount, \$11,479,262 consisted of cash and cash equivalents, \$10,553,360 of investments, \$4,006,003 of construction in progress, and \$5,205,139 of other capital assets, net of depreciation. The change in capital assets consisted of capital outlay of \$4,254,464, net of depreciation of \$366,599. Total liabilities were \$39,157,256 as of year-end, which consisted of \$29,497,418 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, 2018 and 2017, is as follows:

	<u>2018</u>	<u>2017</u>
Other assets	\$ 36,296,307	\$ 41,141,978
Capital assets, net of depreciation	9,211,142	5,323,277
<b>Total Assets</b>	<u>45,507,449</u>	<u>46,465,255</u>
Deferred Charge on Refunding	104,206	124,342
<b>Total Deferred outflows</b>	<u>104,206</u>	<u>124,342</u>
Other liabilities	7,297,340	1,532,969
Long-term liabilities	31,859,916	34,504,692
<b>Total Liabilities</b>	<u>39,157,256</u>	<u>36,037,661</u>
Net position:		
Net investment in capital assets	241,286	(428,371)
Restricted	3,246,852	3,467,122
Unrestricted	2,966,261	7,513,185
<b>Total Net Position</b>	<u>\$ 6,454,399</u>	<u>\$ 10,551,936</u>

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**MANAGEMENT’S DISCUSSION AND ANALYSIS (continued)**

**Government-wide Financial Analysis - continued**

The total net position of the District decreased by \$4,097,537. During the year ended June 30, 2018, net investment in capital assets increased by \$669,657 due to the addition of projects in the construction phase, restricted net position decreased by \$220,270, and unrestricted net position decreased by \$4,546,924 due to spending on capital projects including the reconstruction of Hollyhurst and Post Oak Lane, as well as new pedestrian pylons for Post Oak Boulevard. A comparative summary of the District’s statement of activities for the past two years is as follows:

	<u>2018</u>	<u>2017</u>
<b>Revenues</b>		
Program revenue		
Charges for services	\$ 1,594,207	\$11,292,611
Capital Grants	24,110,736	1,916,832
General revenues		
Property taxes	8,584,757	9,399,737
Unrestricted investment earnings	182,153	116,972
Total Revenues	<u>34,471,853</u>	<u>22,726,152</u>
<b>Expenses</b>		
General and administrative	3,052,265	2,892,047
Traffic control	1,661,312	1,376,900
Maintenance and beautification	1,624,928	1,773,587
Planning and engineering	184,651	144,138
Marketing and communications	800,810	708,936
Interest on long-term debt	782,557	1,003,758
Economic development	36,723	96,941
Construction on behalf of the City of Houston	6,315,408	4,920,456
Transfers to other governments	24,110,736	1,916,832
Total Expenses	<u>38,569,390</u>	<u>14,833,595</u>
Increase (decrease) in net position	(4,097,537)	7,892,557
Net position - beginning	10,551,936	2,659,379
Net position - ending	<u>\$ 6,454,399</u>	<u>\$10,551,936</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 \$20,757,382, a decrease of \$9,866,342 in comparison with the prior year. This is due to spending on capital projects including the reconstruction of Hollyhurst and Post Oak Lane, as well as new pedestrian pylons for Post Oak Boulevard.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**MANAGEMENT’S DISCUSSION AND ANALYSIS (continued)**

**Financial Analysis of the Government’s Funds - continued**

The unassigned portion of fund balance is \$7,539,986 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 \$9,703,708, debt service of \$3,462,139, or is classified as nonspendable.

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

	<u>2018</u>	<u>Increase (Decrease)</u>	<u>2017</u>	<u>Increase (Decrease)</u>	<u>2016</u>
General Fund	\$ 7,591,535	\$ 679,929	\$ 6,911,606	\$ 578,251	\$ 6,333,355
Capital Projects Fund	9,703,708	(10,347,822)	20,051,530	1,262,694	18,788,836
Debt Service Fund	3,462,139	(198,449)	3,660,588	1,299,861	2,360,727
	<u>\$ 20,757,382</u>	<u>\$ (9,866,342)</u>	<u>\$ 30,623,724</u>	<u>\$ 3,140,806</u>	<u>\$ 27,482,918</u>

The General Fund is the chief operating fund of the District. Fund balance in the General Fund increased by \$679,929 during the current fiscal. This increase is due to property tax revenues exceeding operating expenditures. 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 \$7,539,986, while expenditures for the year were \$7,118,547.

The Debt Service Fund has a total fund balance of \$3,462,139, all of which is restricted for the payment of debt service. The decrease in fund balance during the current year in the Debt Service Fund was \$198,449.

The Capital Projects Fund has total fund balance of \$9,703,708. The decrease in the fund balance during the current year in the Capital Projects Fund was \$10,347,822. The decrease is primarily related to capital project spending for Hollyhurst, Post Oak Lane and Post Oak Boulevard.

**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 an increase to fund balance of \$679,929. Variances between budget and actual were due primarily to budget variances in property tax revenues and operational spending.

**Debt Administration**

At June 30, 2018 and 2017, the District had total bonded debt outstanding as shown below:

<u>Series</u>	<u>2018</u>	<u>2017</u>
Series 2013	\$ 5,990,000	\$ 6,870,000
Series 2015	17,830,000	19,040,000
Series 2016	7,700,000	8,150,000
	<u>\$ 31,520,000</u>	<u>\$ 34,060,000</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 70<sup>th</sup> Texas Legislature. The District levies an ad valorem tax on real and personal property within its boundaries. The tax rate for tax year 2017 was \$0.14345 per \$100 of assessed value. The tax rate will remain the same for tax year 2018, 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 17<sup>th</sup> 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 108,000 office employees in the Uptown market area. At the end of the second quarter, 2018 class A office space was 82.4% leased similar to Houston's total Class A office market, also with occupancy at 82.7%.

The 2017 certified values for the office sector were up approximately seven percent from the previous year. This 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. Also, Hanover is adding almost 50,000 SF of office in their new residential tower scheduled to be completed in 2019.

#### **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 2017 were up approximately thirteen percent from the previous year. Retail was 99% leased as of Q2 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.

The area's RevPAR (revenues per available room) for 2018 Q2 is \$107.62 in comparison to the Houston Central Business District at \$134.85. The RevPAR for Houston City-wide is \$73.99. Uptown Houston also boasts one of the highest occupancy rates in the city at 72.2%, while the Houston City-wide occupancy rate was 68.6% at the end of the second quarter, 2018.

## **HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS (*continued*)**

#### **Residential**

In 2017, two new residential projects were delivered to the Uptown market area adding 700 units. In 2018, it is projected that an additional 700 units will come online. This year, three new multi-family projects opened adding more than \$100 million dollars of value to the tax roll. Uptown Houston is one of the most prestigious and desirable areas to live.

The economic outlook is positive and Uptown remains a viable district. 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 No. 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 Harris County Improvement District No. 1, 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, 2018**

**Assets**

Cash and cash equivalents	\$ 11,230,858
Restricted Cash	248,404
Investments	10,553,360
Property taxes receivable	146,454
Due from other governments	14,047,350
Other receivables	18,332
Prepaid items	51,549
Construction in progress	4,006,003
Other capital assets, net of depreciation	5,205,139
Total Assets	<u>45,507,449</u>

**Deferred Outflows of Resources**

Deferred Charge on Refunding	104,206
Total Deferred Outflows of Resources	<u>104,206</u>

**Liabilities**

Accounts payable and accrued expenses	1,769,446
Other payables	224,846
Due to other governments	5,045,998
Accrued interest	257,050
Noncurrent liabilities:	
Due in less than one year	2,619,548
Due in more than one year	29,240,368
Total Liabilities	<u>39,157,256</u>

**Net Position**

Net investment in capital assets	241,286
Restricted for debt service	3,246,852
Unrestricted	2,966,261
Total Net Position	<u>\$ 6,454,399</u>

See notes to the Financial Statements.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**STATEMENT OF ACTIVITIES - GOVERNMENTAL ACTIVITIES**

**For the Year Ended June 30, 2018**

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenue</u>		<u>Net (Expense)</u>
		<u>Charges</u>	<u>Capital</u>	<u>Revenue and</u>
		<u>for</u>	<u>Grants</u>	<u>Changes in</u>
		<u>Services</u>		<u>Net Position</u>
General and administrative	\$ 3,052,265	\$ 1,573,267	\$ -	\$ (1,478,998)
Traffic Control	1,661,312	-	-	(1,661,312)
Maintenance and beautification	1,624,928	20,940	-	(1,603,988)
Planning and engineering	184,651	-	-	(184,651)
Marketing and communication	800,810	-	-	(800,810)
Interest on long-term debt and other charges	782,557	-	-	(782,557)
Economic development	36,723	-	-	(36,723)
Construction on behalf of the City of Houston	6,315,408	-	24,110,736	17,795,328
Transfers to other governments - Uptown Development Authority	24,110,736	-	-	(24,110,736)
<b>Total activities</b>	<u>\$ 38,569,390</u>	<u>\$ 1,594,207</u>	<u>\$ 24,110,736</u>	<u>(12,864,447)</u>

General revenues:	
Property taxes	8,584,757
Unrestricted investment earnings	182,153
Total general revenues and transfers	<u>8,766,910</u>
Change in net position	(4,097,537)
Net position - beginning	<u>10,551,936</u>
Net position - ending	<u>\$ 6,454,399</u>

See notes to the Financial Statements.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**BALANCE SHEET - GOVERNMENTAL FUNDS**

**June 30, 2018**

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
<b>Assets</b>				
Cash and cash equivalents	\$ 7,861,962	\$ 517,514	\$ 2,851,382	\$ 11,230,858
Restricted Cash	248,404	-	-	248,404
Investments	-	10,553,360	-	10,553,360
Taxes receivable	104,691	-	41,763	146,454
Due from other funds	-	-	42,369	42,369
Due from other governments	65,366	4,996,784	8,985,200	14,047,350
Due from others	18,332	-	-	18,332
Prepaid items	51,549	-	-	51,549
Total Assets	<u>\$ 8,350,304</u>	<u>\$ 16,067,658</u>	<u>\$ 11,920,714</u>	<u>\$ 36,338,676</u>
<b>Liabilities and Deferred Inflows</b>				
<b>Liabilities:</b>				
Accounts payable	\$ 297,691	\$ 1,466,667	\$ 5,088	\$ 1,769,446
Due to other funds	-	42,369	-	42,369
Due to other governments	131,541	4,854,914	59,543	5,045,998
Other payables	224,846	-	-	224,846
Total Liabilities	<u>654,078</u>	<u>6,363,950</u>	<u>64,631</u>	<u>7,082,659</u>
<b>Deferred Inflows of Resources</b>				
Unavailable revenues - property taxes	104,691	-	41,763	146,454
Unavailable revenues - developer agreements	-	-	8,352,181	8,352,181
Total Deferred Inflows of Resources	<u>104,691</u>	<u>-</u>	<u>8,393,944</u>	<u>8,498,635</u>
<b>Fund balances:</b>				
Restricted for:				
Nonspendable	51,549	-	-	51,549
Restricted	-	9,703,708	3,462,139	13,165,847
Unassigned	7,539,986	-	-	7,539,986
Total Fund Balances	<u>7,591,535</u>	<u>9,703,708</u>	<u>3,462,139</u>	<u>20,757,382</u>
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	<u>\$ 8,350,304</u>	<u>\$ 16,067,658</u>	<u>\$ 11,920,714</u>	<u>\$ 36,338,676</u>

See notes to the Financial Statements.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**RECONCILIATION OF THE GOVERNMENTAL FUNDS  
BALANCE SHEET TO THE STATEMENT OF NET POSITION**

**June 30, 2018**

**Total fund balance, governmental funds** \$ 20,757,382

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	\$ 4,006,003	
Capital assets at historical cost	19,594,879	
Less accumulated depreciation	<u>(14,389,740)</u>	
Change due to capital assets		9,211,142

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	92,611	
Penalty and interest receivable	<u>53,843</u>	
Change due to property taxes		146,454

Amounts due from project development agreements are due and, but are not available and therefore are deferred in the funds: 8,352,181

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	(31,520,000)	
Deferred charge on refunding	104,206	
Unamortized premiums	(310,628)	
Accrued interest	(257,050)	
Compensated absences	<u>(29,288)</u>	
Change due to long-term obligations		<u>(32,012,760)</u>

**Net Position of Governmental Activities in the Statement of Net Position** \$ 6,454,399

See notes to the Financial Statements.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**STATEMENT OF REVENUES, EXPENDITURES  
AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS**

**For the Year Ended June 30, 2018**

	<b>General Fund</b>	<b>Capital Projects</b>	<b>Debt Service</b>	<b>Total Governmental Funds</b>
<b>Revenues</b>				
Property taxes	\$ 6,172,609	\$ -	\$ 3,178,144	\$ 9,350,753
Intergovernmental	1,573,267	24,110,736	-	25,684,003
Investment earnings	31,660	143,723	6,770	182,153
Other Income	20,940	-	-	20,940
<b>Total Revenues</b>	<b>7,798,476</b>	<b>24,254,459</b>	<b>3,184,914</b>	<b>35,237,849</b>
<b>Expenditures</b>				
Current:				
Planning and engineering	184,651	-	-	184,651
Traffic control	1,376,915	-	-	1,376,915
Maintenance and beautification	1,624,928	-	-	1,624,928
General and administrative	3,097,020	-	-	3,097,020
Marketing and communications	798,310	-	-	798,310
Economic development	36,723	-	-	36,723
Debt Service:				
Principal	-	-	2,540,000	2,540,000
Interest and other charges	-	1,375	843,363	844,738
Capital Outlay	-	10,490,170	-	10,490,170
Transfers to other governments - Uptown Development Authority	-	24,110,736	-	24,110,736
<b>Total Expenditures</b>	<b>7,118,547</b>	<b>34,602,281</b>	<b>3,383,363</b>	<b>45,104,191</b>
Excess (deficiency) of Revenues over Expenditures	679,929	(10,347,822)	(198,449)	(9,866,342)
 Net change in Fund Balances	 679,929	 (10,347,822)	 (198,449)	 (9,866,342)
Fund Balances - beginning of year	6,911,606	20,051,530	3,660,588	30,623,724
Fund Balances - end of year	<u>\$ 7,591,535</u>	<u>\$ 9,703,708</u>	<u>\$ 3,462,139</u>	<u>\$ 20,757,382</u>

See notes to the Financial Statements.

**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, 2018**

Net change in fund balances - total governmental funds: \$ (9,866,342)

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	\$ (132,977)	
Project development agreement revenue	<u>(633,019)</u>	
		(765,996)

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	\$ 4,254,464	
Depreciation expense	<u>(366,599)</u>	
Change due to capital assets		3,887,865

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	2,540,000	
Premium is amortized over the life of the bond	60,021	
Deferred charge on refunding is amortized over the life of the bond	<u>(20,136)</u>	
		2,579,885

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	44,755	
Change in interest payable	<u>22,296</u>	
		<u>67,051</u>
Change in net position of governmental activities		<u><u>\$ (4,097,537)</u></u>

See notes to the Financial Statements.

# HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

## NOTES TO THE FINANCIAL STATEMENTS

June 30, 2018

### 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 70<sup>th</sup> 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, 2018, 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.

<u>Asset</u>	<u>Estimated Useful Lives</u>
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, 2018.

##### 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 \$104,206.

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 property taxes including penalty and interest of \$146,454 that qualifies 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)**

**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, 2018.

These District’s money market mutual funds are reported at fair value using Level 1 inputs and the U.S. Treasury Notes are reported at fair value using Level 2 inputs and all are rated AAA/AA+. The weighted average maturity of the District’s investment portfolio is 144 days. As of June 30, 2018, the District’s investments were comprised of the following:

	<u>Amount</u>
Money Markey Mutual Funds	3,056,390
U.S. Treasury Notes	<u>7,496,970</u>
	<u>\$ 7,496,970</u>

**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.

**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.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**C. Capital Assets**

A summary of changes in capital assets, for the year ended June 30, 2018, follows:

	<b>Beginning Balance</b>	<b>Additions</b>	<b>Retirements and Transfers</b>	<b>Ending Balance</b>
Capital assets, not being depreciated				
Construction in progress	\$ -	\$ 4,006,003	\$ -	\$ 4,006,003
Total Capital assets, not being depreciated	-	4,006,003	-	4,006,003
Capital assets, being depreciated:				
Machinery and equipment	19,346,418	248,461	-	19,594,879
Less accumulated depreciation	(14,023,141)	(366,599)	-	(14,389,740)
Total Capital assets, net of depreciation	5,323,277	(118,138)	-	5,205,139
<b>Governmental Capital Assets</b>	<b>\$ 5,323,277</b>	<b>\$ 3,887,865</b>	<b>\$ -</b>	<b>\$ 9,211,142</b>

Depreciation was charged to functions of the District as follows:

Traffic control	\$ 364,099
Marketing and communication	2,500
Total depreciation expense	<u>\$ 366,599</u>

**D. Long-Term Liabilities**

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

	<b>Beginning Balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending Balance</b>	<b>Due Within One Year</b>
Bonds payable	\$ 34,060,000	\$ -	\$ (2,540,000)	\$ 31,520,000	\$ 2,605,000
Unamortized premiums	370,649	-	(60,021)	310,628	-
Compensated absences	74,043	132,180	(176,935)	29,288	14,548
	<u>\$ 34,504,692</u>	<u>\$ 132,180</u>	<u>\$ (2,776,956)</u>	<u>\$ 31,859,916</u>	<u>\$ 2,619,548</u>

Bonds payable as of June 30, 2018 consists of the following:

<b>Series</b>	<b>Amount Outstanding</b>	<b>Original Issue</b>	<b>Interest Rate</b>
Unlimited Tax Refunding Bonds, Series 2013	\$ 5,990,000	\$ 9,300,000	1.875% - 4.00%
Unlimited Tax Bonds, Series 2015	17,830,000	20,365,000	2.499%
Unlimited Tax Bonds, Series 2016	7,700,000	8,150,000	2.250%
<b>Total</b>	<u>\$ 31,520,000</u>		

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**D. Long-Term Liabilities (continued)**

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.

	<b>Previous</b>		<b>Year End</b>
	<b>Balance</b>	<b>Current Year</b>	<b>Balance</b>
Refunding difference 2013 Issue	<u>\$ 124,342</u>	<u>\$ (20,136)</u>	<u>\$ 104,206</u>
	<u><u>\$ 124,342</u></u>	<u><u>\$ (20,136)</u></u>	<u><u>\$ 104,206</u></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 these outstanding bonds are as follows:

<b>Year Ending</b>			
<b>June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2019	\$ 2,605,000	\$ 774,959	\$ 3,379,959
2020	2,675,000	705,484	3,380,484
2021	2,750,000	634,035	3,384,035
2022	2,820,000	560,629	3,380,629
2023	2,855,000	485,804	3,340,804
2024	2,910,000	404,411	3,314,411
2025	1,890,000	337,730	2,227,730
2026	1,935,000	291,299	2,226,299
2027	1,985,000	243,720	2,228,720
2028	2,035,000	194,928	2,229,928
2029	2,085,000	144,924	2,229,924
2030	2,140,000	93,645	2,233,645
2031	2,190,000	41,092	2,231,092
2032	645,000	7,256	652,256
	<u><u>\$ 31,520,000</u></u>	<u><u>\$ 4,919,916</u></u>	<u><u>\$ 36,439,916</u></u>

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**D. Long-Term Liabilities (continued)**

A summary of District Bonds authorized, but unissued at June 30, 2018 follows:

Purpose	Date Authorized	Amount Authorized	Amount Unissued
Stimulation and development of transportation	05/30/92	\$ 75,000,000	\$ 31,410,000
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>\$ 103,405,000</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.

Property taxes are collected based on rates adopted in the year of the levy. The District's fiscal year ended June 30, 2018, was financed through the 2017 tax levy. The District levied property taxes of per \$100 of assessed value, of which \$0.10125 was allocated to maintenance and operations and \$0.0422 was allocated to debt service. The resulting tax levy was on the adjusted taxable value of \$6,505,084,001.

Taxes receivable, at June 30, 2018, consisted of the following:

Current year taxes receivable	\$ 31,353
Delinquent taxes receivable	<u>61,258</u>
	92,611
Penalty and interest receivable	<u>53,843</u>
Total property taxes receivable	<u>\$ 146,454</u>

The District also recorded an amount due to other governments for tax refunds in the amount of \$191,084. These refunds will be applied against collections in the following fiscal year.

## **HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

### **NOTES TO THE FINANCIAL STATEMENTS *(continued)***

#### **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).

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.



## HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

### NOTES TO THE FINANCIAL STATEMENTS *(continued)*

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

##### **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, 2018). 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, 2018, the District contributed \$127,645 to the plan.

##### **I. Deferred Compensation**

During the fiscal year ended June 30, 2018, 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, 2018, the District contributed \$54,200 to the plan and the amount in the Retirement Plan as of June 30, 2018 is \$248,404.

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**NOTES TO THE FINANCIAL STATEMENTS (continued)**

**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, 2018, the District received \$1,573,267 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, 2018, is shown below along with similar information for the total grant.

<u>Funding Source</u>	<u>Cumulative Amounts</u>	
	<u>Actual through June 30, 2018</u>	<u>Total Grant Awarded</u>
Congestion Mitigation Air Quality Federal (CMAQ) Grant (80%)	\$ 43,827,888	\$ 88,767,462
Congressional Appropriated Discretionary Grant	2,464,244	2,665,864
	<u>\$ 46,292,132</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, 2018, the UDA provided the required local match of \$383,366.

**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, 2018 is \$8,985,200.

## HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

### NOTES TO THE FINANCIAL STATEMENTS *(continued)*

#### **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 are two members of the District board that also serve 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.

As public agencies, the District and the Authority are governed by strict laws and regulations on how property is acquired for public projects.

As of the June 30, 2018 reporting period, the Authority purchased no parcels of land from Directors with interest/affiliation in the parcels. The Authority has chosen to keep the purchase prices for property acquired along Post Oak Boulevard confidential until the Authority closes each parcel, this information is excerpted from disclosure under 552.105 of the Texas Government Code.

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**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, 2018**

	<b>Original Budget</b>	<b>Final Budget</b>	<b>Actual</b>	<b>Variance with Final Budget Positive/ (Negative)</b>
<b>Revenues</b>				
Property taxes	\$ 6,894,568	\$ 6,894,568	\$ 6,172,609	\$ (721,959)
Intergovernmental	1,544,800	1,544,800	1,540,004	(4,796)
Shelter program (Metro)	33,263	33,263	33,263	-
Investment earnings	13,107	13,107	31,660	18,553
Grant proceeds	23,235,000	23,235,000	24,110,736	875,736
Miscellaneous	-	-	20,940	20,940
<b>Total Revenues</b>	<b>31,720,738</b>	<b>31,720,738</b>	<b>31,909,212</b>	<b>188,474</b>
<b>Expenditures</b>				
Current:				
Planning and engineering	130,000	130,000	184,651	(54,651)
Traffic control	1,391,600	1,391,600	1,376,915	14,685
Maintenance and beautification	1,751,014	1,751,014	1,624,928	126,086
General and administrative	3,186,020	3,186,020	3,097,020	89,000
Marketing and communications	756,000	756,000	798,310	(42,310)
Economic development	90,000	90,000	36,723	53,277
Transfer of Grants to UDA	23,235,000	23,235,000	24,110,736	(875,736)
<b>Total Expenditures</b>	<b>30,539,634</b>	<b>30,539,634</b>	<b>31,229,283</b>	<b>(689,649)</b>
 Excess (deficiency) of revenues over expenditures	 1,181,104	 1,181,104	 679,929	 501,175
<b>Other Financing Sources (Uses)</b>				
Transfers out	(1,181,104)	(1,181,104)	-	(1,181,104)
<b>Total Other Financing Sources (uses)</b>	<b>(1,181,104)</b>	<b>(1,181,104)</b>	<b>-</b>	<b>(1,181,104)</b>
 Net change in fund balance	 -	 -	 679,929	 679,929
Fund balance - beginning of year	6,911,606	6,911,606	6,911,606	-
<b>Fund balance - end of year</b>	<b>\$ 6,911,606</b>	<b>\$ 6,911,606</b>	<b>\$ 7,591,535</b>	<b>\$ 679,929</b>

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION**

**June 30, 2018**

**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, 2017, the District adopted its annual budget, or Original Budget, any amendments to the budget are made throughout the year but prior to June 30, 2018 to present a Final Budget as of June 30, 2018. 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. Planning and Engineering expenditures exceeded the budget by \$54,651 due to planning and designs for holiday stars for all District streets excluding Post Oak Boulevard which was conceived after the budget year. Marketing and Communications expenditures exceeded the budget by \$42,310 due to the first Uptown Dine Around promotion which was conceived and implemented after the budget year began to highlight / promote and support Uptown restaurants. Transfers of Grants to UDA exceeded the budget by \$875,736 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 operated with a positive budget variance.



**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, 2018, 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 12, 2018.

**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.

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

Houston, Texas  
December 12, 2018

**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, 2018. 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, 2018.

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.

The image shows a handwritten signature in black ink that reads "Whitley Penn LLP". The signature is written in a cursive, professional style.

Houston, Texas  
December 12, 2018

**HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
**FOR THE YEAR ENDED JUNE 30, 2018**

**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:

<b>Name of Federal Program</b>	<b>CFDA Number</b>
<b>Federal Transit Cluster:</b>	
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, 2018**

**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, 2018**

<b>Federal Grantor/ Pass Through Grantor/ Program Title</b>	<b>CFDA Number</b>	<b>Grantor Number</b>	<b>Federal Grant Expenditures</b>
<b>Department of Transportation</b>			
<b>Direct:</b>			
<b><u>Federal Transit Cluster:</u></b>			
<i>Federal Transit Formula Grants:</i>			
<i>Post Oak Dedicated Bus Lanes/Trst Ctr</i>	20.507	TX-95-Y005-00	\$ 19,860,529
<i>Bellaire Uptown Transit Center</i>	20.507	TX-95-Y005-00	4,250,207
<b>Total Federal Transit Cluster</b>			<u>24,110,736</u>
<b>Total Department of Transportation</b>			<u>24,110,736</u>
<b>Total Federal Awards</b>			<u>\$ 24,110,736</u>

## HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

### NOTES TO THE 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 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, 2018. 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, 2018**

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, 2018**

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

To the Board of Directors of  
Harris County Improvement District No. 1  
1980 Post Oak Boulevard, Suite 1700  
Houston, TX 77056

We have audited the financial statements of Harris County Improvement District No. 1 as of and for the year ended June 30, 2018, and have issued our report thereon dated December 12, 2018. Professional standards require that we advise you of the following matters relating to our audit.

### **Our Responsibility in Relation to the Financial Statement Audit**

As communicated in our engagement letter dated July 9, 2018, our responsibility, as described by professional standards, is to form and express an opinion(s) about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, as part of our audit, we considered the internal control of Harris County Improvement District No. 1 solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

### **Planned Scope and Timing of the Audit**

We conducted our audit consistent with the planned scope and timing we previously communicated to you.

### **Compliance with All Ethics Requirements Regarding Independence**

The engagement team and our firm, including its employees, have complied with all relevant ethical requirements regarding independence. We assisted the District with compiling the financial statements as well as preparing government-wide conversion entries. We identified threats to independence while performing these non-attest services. In order to reduce the threats to an acceptable level, we has a professional staff member not assigned to the engagement team review the work performed. Also, we believe management has the skills, knowledge, and experience to oversee the non-attest services provided.

## **Qualitative Aspects of the Entity's Significant Accounting Practices**

### *Significant Accounting Policies*

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by Harris County Improvement District No. 1 is included in Note A to the financial statements. There have been no initial selection of accounting policies and no changes in significant accounting policies or their application during fiscal year 2018. No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

### *Significant Accounting Estimates*

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's current judgments. Those judgments are normally based on knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgments.

The most sensitive accounting estimates affecting the financial statements is depreciation expense.

Management's estimate of depreciation expense is based on the estimated useful life of capital assets. We evaluated the key factors and assumptions used to develop the depreciation expense estimate and determined that it is reasonable in relation to the basic financial statements taken as a whole and in relation to the applicable opinion units.

### *Financial Statement Disclosures*

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting Harris County Improvement District No. 1's financial statements relate to commitments and contingencies.

## **Significant Difficulties Encountered during the Audit**

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

## **Uncorrected and Corrected Misstatements**

For purposes of this communication, professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that we believe are trivial, and communicate them to the appropriate level of management. Further, professional standards require us to also communicate the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole and each applicable opinion unit. There are no uncorrected misstatements.

In addition, professional standards require us to communicate to you all material, corrected misstatements that were brought to the attention of management as a result of our audit procedures. The attached schedule

consists of material misstatements that we identified as a result of our audit procedures were brought to the attention of, and corrected by, management.

### **Disagreements with Management**

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter, which could be significant to Harris County Improvement District No. 1's financial statements or the auditor's report. No such disagreements arose during the course of the audit.

### **Representations Requested from Management**

We have requested certain written representations from management, which are included in the management representation letter dated December 12, 2018.

### **Management's Consultations with Other Accountants**

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

### **Other Significant Matters, Findings, or Issues**

In the normal course of our professional association with Harris County Improvement District No. 1, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, operating and regulatory conditions affecting the entity, and operational plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as Harris County Improvement District No. 1's auditors.

### **Other Matters**

We applied certain limited procedures to management's discussion and analysis (MD&A) and the Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget to Actual, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the following, which accompany the financial statements but are not RSI:

- 1) Schedule of Expenditures of Federal Awards

With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Our responsibility also includes communicating to you any information which we believe is a material misstatement of fact. Nothing came to our attention that caused us to believe that such information, or its manner of presentation, is materially inconsistent with the information, or manner of its presentation, appearing in the financial statements.

**Restriction on Use**

This report is intended solely for the information and use of the Board of Directors and management of Harris County Improvement District No. 1 and is not intended to be and should not be used by anyone other than these specified parties.

*Whitley Penn LLP*

Houston, Texas  
December 12, 2018

Account	Description	W/P Ref	Debit	Credit
<b>Adjusting Journal Entries JE # 5</b>		<b>4200.90</b>		
Record developer agreement at the fund level.				
3-1240	Due From UDA Developer Agrmt		8,352,181.00	
3-2320	Unavailable Revenue - developer agreement			8,352,181.00
<b>Total</b>			<b>8,352,181.00</b>	<b>8,352,181.00</b>
<b>Adjusting Journal Entries JE # 6</b>		<b>4200.05</b>		
Property tax refunds for June 2018				
1-4305	Ad Valorem - Prior Years Rev.		131,541.00	
3-4305	Ad Valorem/Prior Years Rev.		59,543.00	
1-2604	Due to other governments - property tax refunds			131,541.00
3-2604	Due to other governments - property tax refunds			59,543.00
<b>Total</b>			<b>191,084.00</b>	<b>191,084.00</b>