

MANAGEMENT LETTER

To the Management of the City of Houston, Texas:

In planning and performing our audit of the financial statements of the City of Houston, Texas (the City) as of and for the year ended June 30, 2018, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

However, during our audit we became aware of matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters. We previously communicated to you about the City's internal control in our letter dated November 29, 2018, which contains our communication of significant deficiencies or material weaknesses in the City's internal control. This letter does not affect our report dated November 29, 2018, on the financial statements of the City.

We will review the status of these comments during our next audit engagement. We have already discussed many of these comments and suggestions with various City personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

This communication is intended solely for the information and use of management, and others within the City, and is not intended to be, and should not be, used by anyone other than those specified parties.

November 29, 2018

 

MEMORANDUM ON OPPORTUNITIES FOR STRENGTHENING INTERNAL CONTROLS AND OPERATING EFFICIENCY

A. IMPROVE CONTROL OVER INVESTMENT POOL

In accordance with the City's accounting policy, the majority of the City's cash and investments are administered using a pooled concept, which combines the monies of various funds for investment purposes. Interest earnings of the pool are apportioned to each fund, unless otherwise required by bond covenants, based on the fund's relative share of the investment pool. All cash and investments are displayed on the statement of net position as "Cash and cash equivalents" and "Investments" and in accordance with GASB Statement No. 31 "Accounting and Financial Reporting for Certain Investments and for External Investment Pools".

In our review of the investment pool, we discovered the City does not have a method within its accounting software application, (SAP) to appropriately reconcile each individual fund equity in the investment pool. Because the City's accounting system does not track the activity by each fund, alternative accounting procedures have to be employed to assess the proper investment balance in each of the participating funds.

Recommendation: We recommend that the City complete and review the process that has been developed by Houston IT Services (HITS) to appropriately create and maintain a system within SAP that balances the "investment" and corresponding "equity" accounts for each fund participating in investment pools.

B. IMPROVEMENT ON INTERFUND ACTIVITY

During the audit, we noticed that interfund activity for nonreciprocal and reciprocal activities were being used interchangeably and accordingly, were not properly recorded and classified. Under the accounting principles, nonreciprocal interfund activity comprises interfund transfers and interfund reimbursements, while reciprocal interfund activities comprise interfund loans and interfund services provided and used.

Recommendation: We recommend that the City identify those transactions that meet the definition of interfund activity in line with generally accepted accounting principles, and then properly apply those principles to ensure proper recording and classification. In addition, we recommend HITS develop the proper notification methodology to flag interfund activity when the accounts are not being used appropriately within SAP.

C. IMPROVEMENT ON MARKING INVESTMENTS TO MARKET AND TO RECONCILIATION OF INVESTMENT CONTROL ACCOUNTS TO SUBLEDGER ACCOUNTS ON A QUARTERLY BASIS

The City records the purchase of investments in the general ledger at cost as transactions occur. At year end, adjustments are made to general ledger investment balances (SAP control accounts) to reflect their fair market value (mark to market).

In its investment subledger, the City records and reflects investments at fair market value and prepares quarterly reports from the subsystem in compliance with the provisions of the Texas Public Funds Investment Act Sec. 2256.023. Accordingly, at anytime during the fiscal year and prior to the end of year closeout, there is a difference in amounts reported in the general ledger and the investments subledger.

Recommendation: We recommend that the City mark to market, in the general ledger system, the investments on a quarterly basis since they are required to provide the City's Investment Committee with quarterly reports that reflects the movement the portfolio has experienced in the market each quarter. We believe this would add value to the monthly close process and it demonstrates strong fiscal prudence that the City's General ledger and investments subsidiary ledger reconcile on a quarterly basis.