

# City of Houston, Texas

Report to Management for the  
Year Ended June 30, 2009

# Deloitte.

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December 18, 2009

City of Houston, Texas  
901 Bagby  
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In planning and performing our audit of the financial statements of City of Houston, Texas (the "City") as of and for the year ended June 30, 2009 (on which we have issued our report dated December 18, 2009), in accordance with auditing standards generally accepted in the United States of America, we considered the City's 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 City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting. However, in connection with our audit, we identified, and included in the attached Appendix, deficiencies related to the City's internal control over financial reporting as of June 30, 2009, that we wish to bring to your attention.

We have also issued a separate report to the City, and management, also dated December 18, 2009, which include certain matters involving the Company's internal control over financial reporting that we consider to be a significant deficiency under standards established by the American Institute of Certified Public Accountants.

The definition of a deficiency is also set forth in the attached Appendix.

This report is intended solely for the information and use of the Mayor, Members of City Council, the City Controller, management, and others within the organization and is not intended to be, and should not be, used by anyone other than these specified parties.

Yours truly,

*Deloitte's Touche LLP*

**SECTION I — CONTROL DEFICIENCIES**

We identified, and have included below, control deficiencies involving the City’s internal control over financial reporting as of June 30, 2009, that we wish to bring to your attention:

**A. RECONCILIATION AND REVIEW OF BALANCE SHEET ACCOUNTS**

The City does not regularly reconcile and review accounts receivable accounts. The lack of timely reconciliations and reviews led to the following: (1) adjustments in the classification of receivables (2) overstatement of receivables in certain funds and (3) understatement of receivables in a fund.

The allowance for doubtful accounts related to certain accounts receivables was determined based on old historical collection data that has been carried forward for several years. The City should establish policies and procedures for calculating the allowances based upon historical experience taking into consideration collections in recent years.

The City does not perform consistent reconciliation and review procedures related to all liability accounts. The lack of reconciliation and review led to the understatement of accounts payable and deferred revenue in a number of funds.

The City does not review balance sheet accounts for stale balances. The City should perform a detailed review and analysis of accounts with stale balances that have not changed between years.

**B. WORKING TRIAL BALANCES**

The City prepares its working trial balances based on a period 12 soft-close. A significant number of adjustments were still required to be posted to the working trial balances after the soft-close. The City should review its year-end closing process and evaluate the adjustments posted after the period 12 soft-close to determine the cause of such adjustments and if such adjustments can be processed prior to the period 12 soft-close. In addition, the City should ensure that the working trial balances are closed in a more timely manner.

**C. PROPERTY TAX RECEIVABLE**

The City booked the property tax receivable based upon the August 31, 2009 Harris County Appraisal District’s (“HCAD”) receivable, instead of the June 30, 2009 receivable. This resulted in understating the receivable by approximately \$9.6 million. The City should ensure the receivable is based upon the HCAD June 30 receivable.

**D. FIXED ASSETS**

The City improved upon the understanding and usage of the fixed asset system and subledger during fiscal year 2009. Although the City performs reconciliations and reviews annually, these reconciliations and reviews should be performed more frequently. The lack of frequent reconciliations and reviews caused a delay in timely and accurate fixed asset rollforwards, as well as multiple material revisions of such rollforwards during the audit. Multiple revisions were due in part to the following:

- Late transfers of completed projects out of WIP

- Inaccurate descriptions of assets
- Late recording of retirements
- Erroneous depreciation expense in the year of acquisition
- Fixed asset accruals made in one fund and subsequently paid partially out of another fund

**E. AMBULANCE RECEIVABLE BALANCES**

The City does not reconcile ambulance receivables to a detailed listing provided by the City's outside third-party service provider. Without proper monitoring of receivable balances, it is difficult to monitor the effectiveness of the third-party administrator. The City should perform regular reconciliations of ambulance receivables to the information provided by the City's outside third-party service provider.

**F. RELATED-PARTY TRANSACTIONS**

The City requires certain employees to complete a conflict of interest statement; however, it does not appear that the City is tracking such related-party transactions for disclosure in the City's annual financial report. The City should track related-party transactions for disclosure purposes.

**G. COMPENSATED ABSENCES**

The compensated absences liability report erroneously included 3,179 employees with liabilities that had been previously paid. This caused an overstatement of the compensated absences liability by approximately \$27 million. The City should increase efforts to review the liability report to ensure that only appropriate employees are included.

**H. STREET PAVING LIENS**

The City has not requested City Council approval to levy assessments in over ten years. The City has continued charging and collecting the assessment. The amount being collected is showing in a liability account and has accumulated to over \$1.6 million. The City should request City Council approval to levy assessments.

**I. OPERATING LEASE SCHEDULE**

The City prepares a schedule related to minimum lease revenues for various operating leases for financial reporting purposes that originally included instances of incorrect lease terms and amounts of future lease payments. The City should increase efforts in this area to ensure an accurate and complete lease listing.

## SECTION II — DEFINITION

The definitions of a deficiency, a material weakness, and a significant deficiency that are established in AU 325, *Communicating Internal Control Related Matters Identified in an Audit*, are as follows:

A *deficiency* in internal control over financial reporting 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 deficiency in design exists when (a) a control necessary to meet the control objective is missing or (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met. A deficiency in operation exists when (a) a properly designed control does not operate as designed, or (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A *material weakness* is a deficiency, or combination of deficiencies, in internal control over financial reporting, 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 combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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