SINGLE AUDIT REPORTS

CITY OF NASSAU BAY, TEXAS

For the Year Ended
September 30, 2008

CITY OF NASSAU BAY, TEXAS

SINGLE AUDIT REPORTS

Year Ended September 30, 2008

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

June 3, 2009

To the Honorable Mayor and
Members of City Council
City of Nassau Bay, Texas

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Nassau Bay, Texas (the "City"), as of and for the year ended September 30, 2008, which collectively comprise the City's basic financial statements and have issued our report thereon dated June 3, 2009. We conducted our audit in accordance with generally accepted auditing standards in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the 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 would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs, items 2008-1 and 2008-2, 2007-1 through 2007-5 and 2007-8 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above we consider items 2008-1, 2007-1 through 2007-3, and 2007-5 to be a material weakness in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain other matters that we reported to management of the City in a separate letter dated June 3, 2009.

The City's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

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

Belt Harris & Associates, LLLP

Belt Harris & Associates, LLLP
Certified Public Accountants
Houston, Texas

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM, INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133, AND SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 3, 2009

To the Honorable Mayor and
Members of City Council
City of Nassau Bay, Texas

Compliance

We have audited the compliance of the City of Nassau Bay, Texas (the "City"), with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2008. The City's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

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

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2008.

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Internal Control Over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 City's internal control over compliance.

A control deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

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

The City's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Nassau Bay, Texas (the "City"), as of and for the year ended September 30, 2008, and have issued our report thereon dated June 3, 2009. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

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

Belt Harris & Associates, LLLP

Belt Harris & Associates, LLLP
Certified Public Accountants
Houston, Texas

CITY OF NASSAU BAY, TEXAS

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended September 30, 2008

No prior findings.

CITY OF NASSAU BAY, TEXAS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended September 30, 2008

A. SUMMARY OF AUDIT RESULTS

1. The auditors' report expresses an unqualified opinion on the basic financial statements of the City of Nassau Bay, Texas.

2. Significant deficiencies in internal control were disclosed by the audit of the basic financial statements, some of which were considered to be a material weakness.

3. No instances of noncompliance material to the basic financial statements were disclosed during the audit.

4. No significant deficiencies in internal control over major federal award programs were disclosed by the audit.

5. The auditors' report on compliance for the major federal award programs expresses an unqualified opinion.

6. No audit findings relative to the major federal award programs for the City are reported in Part C of this schedule.

7. The programs included as major programs included:

	CFDA number
a. Hurricane Ike	97.036

8. The threshold for distinguishing Type A and B programs was $300,000.

9. The City did not classify as a low-risk auditee in the context of OMB Circular A-133.

B. FINDINGS – BASIC FINANCIAL STATEMENT AUDIT

Material Weakness:

2008-1. MUNICIPAL COURT

Finding

In the prior year, we noted various deficiencies within the municipal court. In the current year we have expanded our procedures and findings. We noted that the court does not make daily cash deposits of monies collected and the time between deposits can range from days to weeks. We also noted that fine amounts were not included on the citations themselves, court dates were not always written on tickets, and violation codes printed from the in-car ticket system did not match violation codes in municipal court software.

Violations were not present in the court's software (ex. Nuisance Animals and Sex Offender Ordinance Violation) or incorrect fines were listed and required court costs to be manually added. Also, there were various instances where the base fine amount noted in the court record did not match the fine schedule.

At present, the court clerk is manually handwriting all receipts for payment and entering these payments into the court software rather than directly entering the information and producing a computer generated receipt. In addition, while counting the clerk's cash drawer, it was found to be six dollars short and had checks dated several days after the current date. In the court chambers, there is no access to either the court computer system or ticket printer making it impossible for the court clerk to utilize the court software and issue a computer generated receipt.

Manual receipts are also written by officers at the jail when defendants pay a fine or post a cash bond. There are two receipt books at the jail, both of which had receipts that were skipped and not voided. In addition, receipt amounts did not always match amounts deposited by the court clerk and were not always deposited in a timely manner. In one instance, a receipt was issued for $240 and only $140 was deposited approximately a month later. Then deposit of another $100 was made the following month.

Instances where there was no signature by the judge on warrants issued and cases dismissed were noted. Also noted were instances where warrants were issued by the court but were not entered into SETSIC. As a result, officers would be unaware of an outstanding warrant should they have contact with the subject at a later time. In addition, instances were revealed during the interview process where defendants who had paid their fines were later arrested on nonpayment warrants indicating that warrants were also not removed from SETSIC in a timely manner or that funds had been misappropriated. We also noticed a significant lag between a failure to appear and the issuing of a warrant.

Payment plans did not seem to be either signed or authorized by the judge or kept current. We also noted instances where items were entered in pencil on official records rather than in ink.

The apparent lack of a comprehensive filing system was noted. Files were not organized by alphabetical order, date order, or docket number, instead the court files largely consisted of colored plastic boxes for various situations and were neither complete or in an easily accessible order.

Finally, physical security deficiencies were noted within the court clerk's office. The office of the court clerk is a separate office with no connecting doors to the main offices of the City. The court clerk works alone in this room with no counter or glass to separate the court clerk from people conducting

transactions or cameras to maintain surveillance within this department.

Recommendation

The court should make daily cash deposits. We recommend that the in-car ticket system be changed to automatically print fine amounts and court dates on the face of the ticket if possible. We also recommend that the violation codes in the in-car system be made to match those found in the court software and that signed copies of all citations be maintained by the court.

All violations and their fine amounts should be entered into the court software and should be checked regularly for accuracy and completeness and fine amounts on court records should be checked against this list.

The City should require that computer generated receipts be generated for all payments received by the court clerk. Once information is entered into the City's court software a record is made that cannot be deleted.

The City should also consider requiring that payment plans be approved by the judge and that a system be set up to ensure payment plans are either kept up to date or warrants are issued in a timely manner.

The judge is the only person allowed to declare whether a ticket is dismissed or to issue a warrant. The reason for the dismissal should be properly documented and a written signature from the judge should be obtained. In addition, warrants should be added to, and removed from, SETSIC in a timely manner. The City should also consider hiring a warrant officer to attempt to collect a portion of the large amount of outstanding warrants. Warrants should also be issued in a timely manner upon the failure of a defendant to appear.

The City should require that the date of disposition accurately reflect the date it occurred and that the court clerk change the date in the system rather than handwriting it on the form over the original date. Also any item entered into an official record should be written in indelible ink rather than pencil which could be erased or changed at a later date. A comprehensive filing system that could be easily accessed by all City staff is highly recommended.

The City should reconcile the court cash drawer daily and secure the cash drawer in a fireproof box or safe for overnight safekeeping.

Management's Response

As of May 28, 2009, the operation of the City of Nassau Bay Municipal Court was suspended. The City of Nassau Bay has an existing agreement with the City of Webster for jail and communications services and is presently seeking to expand this agreement to include Municipal Court services.

Significant Deficiencies:

2008-2. ACCOUNTING RECORDS AND DOCUMENTATION

Finding

During our testing of accounts payable, one of the invoices selected for our sample could not be located by staff.

Recommendation

The City should retain copies of all invoices and other documentation.

Management's Response

The City is planning on implementing a capability of the STW software that would allow us to scan in and store supporting documentation within the system. This should make supporting documents more easily accessible and should be as secure as the accounting records. Since this will not be implemented until September 1, 2009, it will therefore provide the greatest impact in the fiscal year 2010 audit.

MATTERS PREVIOUSLY REPORTED

Material Weaknesses:

2007-1. FINANCIAL STATEMENT PRESENTATION

Finding

The City has engaged a licensed certified public accounting firm to prepare and audit the City's annual financial report. The City ensures the quality of its annual financial report by engaging a qualified audit firm with particular expertise in governmental audits and reading a preliminary draft of the report. The City does not have specific controls in place to separately review the selection and application of accounting principles and resulting disclosures and presentations within the financial statement. Although it is common within the government sector and most private companies to rely on their audit firm for these services, an audit firm cannot be considered part of its client's internal control by professional standards currently in effect. Since some presentations and disclosures may be material to the financial statement, this weakness in internal control would be classified as material.

Recommendation

The City should continue to read its annual financial report and ensure the quality of both the document and the preparer. No changes in operation are recommended.

Management's Response

The City should be preparing the financial statements in accordance with GAAP no later than the fiscal year 2010 audit.

2007-2. ACCOUNTING RECORDS AND ADJUSTMENTS

Finding

The City reviews its accounting information and compares the information to their knowledge of historical events. From time to time the auditor recommends adjustments to these records, as well as proposes other adjustments needed for preparing full accrual statements in compliance with GASB 34 which are only needed at year end. Although it is common within the government sector and most private companies to rely on their audit firm for these services, an audit firm cannot be considered part of its client's internal control by professional standards currently in effect (SAS No. 112 effective year ends on or after December 15, 2006). Since some adjustments and calculations made by the auditor may be material to the financial statements, this weakness in internal control would be classified as material.

Recommendation

The City should continue to read its annual financial report and ensure the quality of both the document and the preparer. No changes in operation are recommended.

Management's Response

No changes in operation are planned at this time.

2007-3. SEGREGATION OF DUTIES

Background

Segregation of duties refers to assigning tasks among personnel so that no one person handles substantially all aspects of any transaction. The extent to which the City can segregate duties is limited based on the number of personnel, their skill set and work load, and the organizational structure of the City.

Finding

As with other organizations of the same staff size, there are instances where additional controls could be put in place if more personnel were available and further segregation in duties could be achieved. While the City's segregation of duties appears reasonable given the number of personnel there are some inherent risks given the City's staff size.

Recommendation

The City should continue to evaluate opportunities for greater segregation of duties.

Management's Response

During the current year, the City has taken steps and will continue to look for opportunities for greater segregation of duties.

2007-5. INTERNAL CONTROL (UTILITY BILLING)

Finding

The City's utility billing clerk accepts all utility receipts, issues all utility bills, and makes all utility account adjustments. There are no controls to prevent the utility billing clerk from accepting payments from customers and then adjusting their accounts to zero.

Recommendation

The City should consider dividing the responsibilities of accepting payment and making account adjustments. The City should also require supervisor approval for all adjustments or those that are over a certain dollar amount.

Management's Response

Presently, adjustments require supervisory approval. The City will continue to implement detection controls in an attempt to mitigate this risk.

Significant Deficiencies:

2007-4. RISK ASSESSMENT

Finding

Like many organizations of its size and complexity the City does not have a formal process for assessing risk associated with key controls related to its financial operations and fraud. In addition, while a number of processes are used to communicate internal controls (such as formal actions taken by the City Council, policies and procedures, memos, and controlling legislation), a single source such as a complete and up-to-date policy and procedures manual does not exist. Likewise, the entity does not have a formal process for monitoring its internal control.

Recommendation

The City should continue to monitor the need for more formally established processes to assess risk, communicate controls, and monitor controls. The City might consider at some point having an annual workshop with City Council and management to specifically discuss risk and key controls to mitigate those risks. The City's assessment of its risk and evaluation of the effectiveness of control can then be utilized to determine the sufficiency of the level of documentation.

Management's Response

The City has developed and will continue to develop written policies and procedures to assess and reduce risk.

2007-8. CUSTOMER DEPOSITS

Finding

The City has not adopted an official policy regarding utility deposits. The City code defines rates and

charges, but does not address deposits. As a result the City has not been consistent in requiring utility deposits.

Recommendation

The City should consider formally adopting a deposit policy for their water and sewer customers.

Management's Response

The STW software and customer profiles have been updated to assist with maintaining customer deposit and refund logs. Also, the customer database has been organized according to residential, commercial, public, and institutional water usage to assist with reporting and analysis. The City will develop a written Utility Policy in accordance with Sec. 402.0025 of Local Government Code Municipal Utilities.

C. FINDINGS – FEDERAL AWARDS

None

CITY OF NASSAU BAY, TEXAS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended September 30, 2008

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	FEDERAL CFDA NUMBER	PASS-THROUGH ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
DEPARTMENT OF HOMELAND SECURITY			
Pass-through Texas Department of Public Safety's Division of Emergency Management			
Hurricane Ike	97.036	201-76948-00	$ 614,367
TOTAL DEPARTMENT OF HOMELAND SECURITY			614,367
TOTAL FEDERAL AWARDS EXPENDED			$ 614,367

CITY OF NASSAU BAY, TEXAS

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended September 30, 2008

1. REPORTING ENTITY

The accompanying schedule of expenditures of federal awards presents the activity of all federal financial assistance programs of the City of Nassau Bay, Texas.

2. BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.