

GALVESTON COUNTY, TEXAS

FEDERAL SINGLE AUDIT REPORT

**Fiscal Year Ended
September 30, 2018**

GALVESTON COUNTY, TEXAS

FEDERAL SINGLE AUDIT REPORT

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**INDEPENDENT AUDITORS' 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 Honorable County Judge and
Members of the Commissioners Court
Galveston County, Texas

We have audited, in accordance with the 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, each major fund, and the aggregate remaining fund information of Galveston County, Texas (the "County"), as of and for the year ended September 30, 2018, and the related notes to the financial statements, which collectively comprise the County's basic financial statements, and have issued our report thereon dated March 26, 2019.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the County'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 County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County'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 over financial reporting 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 financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did identify a deficiency in internal control, described in the accompanying *schedule of findings and questioned costs*, that we consider to be a material weakness (Item 2018-001).

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the County'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*.

Galveston County's Response to Findings

Galveston County's response to the findings identified in our audit are described in the accompanying *schedule of findings and questioned costs*. The County's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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 County's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Pattillo, Brown & Hill, L.L.P.

Waco, Texas
March 26, 2019

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR
FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH THE *UNIFORM GUIDANCE***

To the Honorable County Judge and
Members of the Commissioners Court
Galveston County, Texas

Report on Compliance for Each Major Federal Program

We have audited the compliance of Galveston County, Texas (the "County"), with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Compliance Supplement* that could have a direct and material effect on each of the County's major federal programs for the year ended September 30, 2018. The County's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the County's major federal programs 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 (CFR) 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 County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

OFFICE LOCATIONS

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the County's compliance.

Opinion on Each Major Federal Program

In our opinion, the County complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2018.

Report on Internal Control over Compliance

Management of the County 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 County's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program as a basis for designing 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 the *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 County'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.

Report on Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Galveston County, Texas, as of and for the year ended September 30, 2018, and the related notes to the financial statements, which collectively comprise the County's basic financial statements. We issued our report thereon dated March 26, 2019, which contained unmodified opinions on those financial statements. Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the audit requirements of the *Uniform Guidance* and is not a required part of the basic financial statements. Such information 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. The information has been subjected to the auditing procedures applied in the audit of the 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.

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.

Pattillo, Brown & Hill, L.L.P.

Waco, Texas

May 28, 2019, except for our opinion on the Schedule of Expenditures of Federal Awards, for which the date is March 26, 2019

GALVESTON COUNTY, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Total Federal Expenditures	Passed Through to Subrecipients
<u>U.S. Department of Agriculture</u>				
<i>Passed through the Texas Department of Agriculture:</i>				
National School Lunch Program	10.555	N/A	\$ 50,139	\$ -
<i>Total Child Nutrition Cluster</i>			<u>50,139</u>	<u>-</u>
<i>Total Passed through the Texas Department of Agriculture</i>			<u>50,139</u>	<u>-</u>
Total U.S. Department of Agriculture			<u>50,139</u>	<u>-</u>
<u>U.S. Department of Housing and Urban Development</u>				
<i>Passed through the Texas General Land Office:</i>				
Community Development Block Grants - Non-Housing Grant	14.228	DRS010052	174,569	-
Community Development Block Grants - Housing Grant	14.228	72121014	3,383,747	-
Community Development Block Grants - Non-Housing Grant	14.228	DRS220052	<u>4,589,270</u>	<u>-</u>
<i>Total Passed through the Texas General Land Office</i>			<u>8,147,586</u>	<u>-</u>
Total U.S. Department of Housing and Urban Development			<u>8,147,586</u>	<u>-</u>
<u>U.S. Department of Justice</u>				
<i>Direct:</i>				
Edward Byrne Memorial Justice Assistance Grant Program	16.738	2015-DJ-BX-0834	<u>7,941</u>	<u>-</u>
<i>Total Direct Programs</i>			<u>7,941</u>	<u>-</u>
<i>Passed through the Office of the Governor - Texas Criminal Justice Division:</i>				
Law Enforcement Equipment Upgrade Project	16.738	3272701	<u>29,850</u>	<u>-</u>
<i>Subtotal CFDA 16.738</i>			<u>37,791</u>	<u>-</u>
Victims of Crime Act Program (VOCA)	16.575	2550005	83,003	-
Violence Against Women Formula Grants - Prosecutor	16.588	2704105	62,830	-
Violence Against Women Formula Grants - Prosecutor	16.588	2704106	5,648	-
Violence Against Women Formula Grants - Protective Order Attorney	16.588	3111102	<u>60,849</u>	<u>-</u>
<i>Subtotal CFDA 16.588</i>			<u>129,327</u>	<u>-</u>
<i>Total Passed through the Office of the Governor - Texas Criminal Justice Division</i>			<u>242,180</u>	<u>-</u>
Total U.S. Department of Justice			<u>250,121</u>	<u>-</u>
<u>U.S. Department of Health and Human Services</u>				
<i>Passed through the Houston-Galveston Area Council:</i>				
Supportive Services III-B	93.044	AAA17-000280	118,386	-
Congregate & Home Delivered Meal Program III-C	93.045	AAA17-000280	<u>140,898</u>	<u>-</u>
<i>Total Aging Cluster</i>			<u>259,284</u>	<u>-</u>
<i>Total Passed through the Houston-Galveston Area Council</i>			<u>259,284</u>	<u>-</u>

GALVESTON COUNTY, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2018

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Total Federal Expenditures	Passed Through to Subrecipients
<u>U.S. Department of Health and Human Services (continued)</u>				
<i>Passed through the Texas Department of Family and Protective Services:</i>				
Foster Care Title IV-E	93.658	23940068	\$ 30,150	\$ -
Foster Care Title IV-E	93.658	23940070	<u>136,447</u>	<u>-</u>
<i>Total Passed through the Texas Department of Family and Protective Services</i>			<u>166,597</u>	<u>-</u>
Total U.S. Department of Health and Human Services			<u>425,881</u>	<u>-</u>
<u>U.S. Department of Homeland Security</u>				
<i>Passed through the Texas Department of Public Safety:</i>				
Emergency Management Assistance/IKE	97.036	FEMA 1791-DR-TX	1,815,082	-
Emergency Management Performance Grant	97.042	18TX-EMPG-0334	<u>61,676</u>	<u>-</u>
<i>Total Passed through the Texas Department of Public Safety</i>			<u>1,876,758</u>	<u>-</u>
<i>Passed through the Governor's Division of Emergency Management:</i>				
Urban Area Security Initiative 2016 - Regular Solicitation (HAM Radio Kit)	97.067	3168401	4,770	-
Urban Area Security Initiative 2016 - Regional Planner	97.067	2972302	20,193	-
Urban Area Security Initiative 2017 - Regional Planner	97.067	2972303	55,497	-
Urban Area Security Initiative 2016 - UASI CP	97.067	2972202	20,662	-
Urban Area Security Initiative 2017 - UASI CP	97.067	2972203	52,939	-
Urban Area Security Initiative 2017 - UASI M&A	97.067	2986203	<u>873</u>	<u>-</u>
<i>Total Passed through the Governor's Division of Emergency Management</i>			<u>154,934</u>	<u>-</u>
<i>Passed through the Texas Water Development Board:</i>				
Severe Repetitive Loss Program	97.110	TWDB-1200011417	<u>109,018</u>	<u>-</u>
<i>Total Passed through the Texas Water Development Board</i>			<u>109,018</u>	<u>-</u>
Total U.S. Department of Homeland Security			<u>2,140,710</u>	<u>-</u>
Total Federal Awards			<u>\$ 11,014,437</u>	<u>\$ -</u>

The accompanying notes are an integral part of this schedule.

GALVESTON COUNTY, TEXAS

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

SEPTEMBER 30, 2018

Note 1 - Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal grant activity of the County under programs of the federal government for the year ended September 30, 2018. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) 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 County, it is not intended and does not present the financial position, changes in net position/fund balance or cash flows of the County.

Note 2 - Summary of Significant Accounting Policies

Galveston County, Texas, 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 certain compensated absences, claims and judgments, which are recognized when the obligations are expected to be liquidated with expendable available financial resources. Equipment purchases 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 revenue until earned. Generally, unused balances are returned to the grantor at the close of specified project periods.

Note 3 - Indirect Costs

The County has elected not to use the 10% de minimis indirect cost rate as allowed in the *Uniform Guidance*.

GALVESTON COUNTY, TEXAS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FOR THE YEAR ENDED SEPTEMBER 30, 2018

Item 2018-001

Criteria: The objectives of internal control include providing reasonable assurance for the safeguarding of assets.

Condition: In fiscal year 2018, the County fell victim to a “man in the middle” fraud scheme. In this case, the attacker deceived a County employee into believing he/she was communicating with an existing valid vendor. The attacker then also misled the existing valid vendor into believing he/she was communicating with a valid County employee.

The attacker was then able to successfully have the County establish an Automated Clearing House / Electronic Funds Transfer (ACH/EFT) payment channel to the attacker’s bank account rather than the valid vendor’s bank account.

Cause: The factors contributing to this event include:

- inadequate vendor information establishment/change validation processes
- a lack of understanding/training as to recognition of these types of attacks
- a lack of understanding as to which office/department had the responsibility for validation of vendor information.

Effect: The County made a payment of \$525,282 to an entity disguised as a valid existing vendor.

Recommendation:

Prevention of these types of fraud schemes starts with periodic training regarding various aspects of how to recognize these attacks. Additionally, processes for vendor information validation should be clearly defined.

Technology may also assist with the prevention of these types of attacks. For example, there are various products that perform a validation of vendor ACH/EFT information against national database information targeted at identifying an inconsistency in routing numbers and account numbers. There are also software products that can identify email address inconsistencies that can be recognized at the initial point of entry into County email communications. The County may want to perform a cost/benefit analysis on these types of technologies.

Management's Response:

Since the man in the middle attack that began in March 2018, the Department of Information Technology (IT) has offered training on how to recognize these attacks. For those who were not able to attend, it is the intention of the Department of IT to make a recorded version of the training available. Furthermore, the staff of the Auditor's Office is participating in the cybersecurity training sessions offered by the Texas Association of Counties. We have recommended this training to other County officials in addition to the training offered by the Department of IT.

The County is aware that technology does exist that could assist with the prevention of these types of attacks. The Department of IT is currently looking at different systems available to identify email inconsistencies as well as having already implemented systems to identify and block fraudulent emails. Furthermore, the County is currently reviewing the contract with a third-party company who offers a product to verify emails, bank accounts, contact information, etc.

In addition to the aforementioned, the County has taken the additional steps and added controls where the Auditor's Office identified weaknesses:

- a) Vendor master changes are now verified with the original information provided by the vendor by the Purchasing Department,
- b) EFT changes on vendor master files are audited by the Auditor's Office to ensure proper verification was performed prior to payment release, and
- c) EFT changes in payroll are audited by the Auditor's Office to ensure proper verification was performed prior to payment release.

GALVESTON COUNTY



Office of County Auditor

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SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

FOR THE YEAR ENDED SEPTEMBER 30, 2018

None