

**Houston Advanced Research Center**

Consolidated Financial Statements  
and Single Audit Reports  
for the year ended December 31, 2016

# Houston Advanced Research Center

## Table of Contents

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	Page
<b>Independent Auditors' Report</b>	1
<b>Financial Statements:</b>	
Consolidated Statements of Financial Position as of December 31, 2016 and 2015	3
Consolidated Statement of Activities for the year ended December 31, 2016	4
Consolidated Statement of Activities for the year ended December 31, 2015	5
Consolidated Statements of Cash Flows for the years ended December 31, 2016 and 2015	6
Notes to Consolidated Financial Statements for the years ended December 31, 2016 and 2015	7
<b>Supplementary Information:</b>	
Schedule of Expenditures of Federal Awards for the year ended December 31, 2016	11
Note to Schedule of Expenditures of Federal Awards for the year ended December 31, 2016	14
<b>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 <i>Government Auditing Standards</i></b>	15
<b>Independent Auditors' Report on Compliance for Each Major Program and Report on Internal Control Over Compliance Required by the Uniform Guidance</b>	17
Schedule of Findings and Questioned Costs for the year ended December 31, 2016	19

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## Independent Auditors' Report

To the Board of Directors of  
Houston Advanced Research Center:

### Report on the Financial Statements

We have audited the accompanying financial statements of Houston Advanced Research Center, which comprise the consolidated statements of financial position as of December 31, 2016 and 2015 and the related consolidated statements of activities and of cash flows for the years then ended, and the related notes to the financial statements.

### *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.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 our audits to obtain reasonable assurance about whether the financial statements are free from 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 auditors' 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 opinion.

## ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Houston Advanced Research Center as of December 31, 2016 and 2015 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Supplementary Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information included in the schedule of expenditures of federal awards for the year ended December 31, 2016 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* is presented for purposes of additional analysis and is not a required part of the consolidated 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 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 financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

## **Report Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated September 12, 2017 on our consideration of Houston Advanced Research Center'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 solely 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 the effectiveness of Houston Advanced Research Center's 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 Houston Advanced Research Center's internal control over financial reporting and compliance.

*Blazek & Vetterling*

September 12, 2017

## Houston Advanced Research Center

Consolidated Statements of Financial Position as of December 31, 2016 and 2015

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	<u>2016</u>	<u>2015</u>
ASSETS		
Cash	\$ 161,323	\$ 568,202
Accounts receivable	1,107,675	1,800,471
Prepaid expenses and other assets	100,973	66,716
Operating pledges receivable		290,000
Pledges receivable restricted for capital campaign projects		1,850,000
Property and equipment, net ( <i>Note 2</i> )	<u>6,237,585</u>	<u>1,802,405</u>
<b>TOTAL ASSETS</b>	<b><u>\$ 7,607,556</u></b>	<b><u>\$ 6,377,794</u></b>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	\$ 792,681	\$ 874,552
Construction payable	775,820	
Accrued expenses	121,320	121,252
Deferred revenue	3,325	220,016
Notes payable ( <i>Note 3</i> )	<u>2,387,304</u>	<u>817,556</u>
Total liabilities	<u>4,080,450</u>	<u>2,033,376</u>
Net assets:		
Unrestricted	199,040	1,213,901
Temporarily restricted ( <i>Note 4</i> )	<u>3,328,066</u>	<u>3,130,517</u>
Total net assets	<u>3,527,106</u>	<u>4,344,418</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b><u>\$ 7,607,556</u></b>	<b><u>\$ 6,377,794</u></b>

*See accompanying notes to consolidated financial statements.*

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## Houston Advanced Research Center

Consolidated Statement of Activities for the year ended December 31, 2016

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	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>TOTAL</u>
REVENUE:			
Research contracts and grants <i>(Note 5)</i>	\$ 3,048,507		\$ 3,048,507
Contributions	1,515,372	\$ 546,589	2,061,961
Loss on sale of property and equipment	(62,867)		(62,867)
Other income	<u>8,791</u>	<u>                    </u>	<u>8,791</u>
Total revenue	4,509,803	546,589	5,056,392
Net assets released from restrictions:			
Satisfaction of program restrictions	<u>349,040</u>	<u>(349,040)</u>	<u>                    </u>
Total	<u>4,858,843</u>	<u>197,549</u>	<u>5,056,392</u>
EXPENSES:			
Program expenses:			
Energy and Building Solutions	2,402,366		2,402,366
Environment	<u>1,445,046</u>		<u>1,445,046</u>
Total program expenses	3,847,412		3,847,412
Management and general	<u>2,026,292</u>		<u>2,026,292</u>
Total expenses	<u>5,873,704</u>		<u>5,873,704</u>
CHANGES IN NET ASSETS	(1,014,861)	197,549	(817,312)
Net assets, beginning of year	<u>1,213,901</u>	<u>3,130,517</u>	<u>4,344,418</u>
Net assets, end of year	<u>\$ 199,040</u>	<u>\$ 3,328,066</u>	<u>\$ 3,527,106</u>

*See accompanying notes to consolidated financial statements.*

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## Houston Advanced Research Center

Consolidated Statement of Activities for the year ended December 31, 2015

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	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>TOTAL</u>
REVENUE:			
Research contracts and grants <i>(Note 5)</i>	\$ 5,187,757		\$ 5,187,757
Contributions	1,815,779	\$ 179,232	1,995,011
Other income	<u>18,290</u>		<u>18,290</u>
Total revenue	7,021,826	179,232	7,201,058
Net assets released from restrictions:			
Satisfaction of program restrictions	<u>350,321</u>	<u>(350,321)</u>	
Total	<u>7,372,147</u>	<u>(171,089)</u>	<u>7,201,058</u>
EXPENSES:			
Program expenses:			
Energy and Building Solutions	3,119,564		3,119,564
Environment	<u>2,132,049</u>		<u>2,132,049</u>
Total program expenses	5,251,613		5,251,613
Management and general	2,062,963		2,062,963
Fundraising	<u>15,600</u>		<u>15,600</u>
Total expenses	<u>7,330,176</u>		<u>7,330,176</u>
CHANGES IN NET ASSETS	41,971	(171,089)	(129,118)
Net assets, beginning of year	<u>1,171,930</u>	<u>3,301,606</u>	<u>4,473,536</u>
Net assets, end of year	<u>\$ 1,213,901</u>	<u>\$ 3,130,517</u>	<u>\$ 4,344,418</u>

*See accompanying notes to consolidated financial statements.*

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## Houston Advanced Research Center

### Consolidated Statements of Cash Flows for the years ended December 31, 2016 and 2015

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	<u>2016</u>	<u>2015</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Changes in net assets	\$ (817,312)	\$ (129,118)
Adjustments to reconcile changes in net assets to net cash used by operating activities:		
Contributions restricted for capital campaign projects	(461,589)	(14,232)
Loss on sale of property and equipment	62,867	
Depreciation	82,716	78,539
Changes in operating assets and liabilities:		
Accounts receivable	692,796	278,309
Prepaid expenses and other assets	(34,257)	41,018
Operating pledges receivable	290,000	190,000
Accounts payable	(81,871)	(683,030)
Accrued expenses	68	(165,074)
Deferred revenue	<u>(216,691)</u>	<u>115,220</u>
Net cash used by operating activities	<u>(483,273)</u>	<u>(288,368)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(2,257,485)	(488,882)
Proceeds from sale of property and equipment	<u>22,290</u>	<u>          </u>
Net cash used by investing activities	<u>(2,235,195)</u>	<u>(488,882)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from contributions restricted for capital campaign projects	2,311,589	14,232
Repayment of notes payable	<u>          </u>	<u>(150,000)</u>
Net cash provided (used) by financing activities	<u>2,311,589</u>	<u>(135,768)</u>
NET CHANGE IN CASH	(406,879)	(913,018)
Cash, beginning of year	<u>568,202</u>	<u>1,481,220</u>
Cash, end of year	<u>\$ 161,323</u>	<u>\$ 568,202</u>
<i>Supplemental disclosure of cash flow information:</i>		
Purchases of property and equipment funded by notes payable	\$1,569,748	
Purchases of property and equipment funded by construction payable	\$775,820	
Interest paid	\$8,286	\$6,707

*See accompanying notes to consolidated financial statements.*

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## Houston Advanced Research Center

Notes to Consolidated Financial Statements for the years ended December 31, 2016 and 2015

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### NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization – Houston Advanced Research Center (the Center), a Texas nonprofit corporation, is a university-affiliated organization focusing on research in human and ecosystem well-being. Major research interests are in the areas of the environment, energy, and policy analysis. The primary source of funding is research grants and contracts from both public and private sources. Philanthropic support provides funds for internal research and for expenditures not recovered from sponsored research activities.

HARC Technology, Inc. (HTI) is a wholly-owned subsidiary of the Center formed for the purpose of facilitating the transfer of promising technologies from the laboratory to the private sector.

Basis of consolidation – These consolidated financial statements include the assets, liabilities, net assets and activities of the Center and HTI (collectively HARC). All significant intercompany balances and transactions have been eliminated in consolidation.

Federal income tax status – The Center is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(2).

Cash – Bank deposits at December 31, 2015 exceed the federally insured limit per depositor per institution.

Pledges receivable that are due within one year are reported at net realizable value. Pledges receivable that are expected to be collected in future years are discounted to estimate the present value of future cash flows, if material.

Property and equipment is reported at cost, if purchased, or at fair value at the date of gift, if donated. Additions and improvements with a cost of more than \$5,000 are capitalized. Depreciation is provided using the straight-line method over estimated useful lives of 3 to 5 years for furniture and equipment and 10 to 31 ½ years for leasehold improvements.

Net asset classification – Contributions and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations even though their use may be limited in other respects such as by contract or board designation.
- *Temporarily restricted net assets* include contributions restricted by the donor for specific purposes or future time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.

Research contracts and grants are recognized as revenue when the related services are provided. Amounts received in advance are reported as deferred revenue.

Contributions are recognized as revenue at fair value when an unconditional commitment is received from the donor. Contributions received with donor stipulations that limit their use are classified as restricted support. Conditional promises to give are recognized in the same manner when the conditions are substantially met. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are classified as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Center reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service. During 2016, HARC received \$1,900,000 in contributions from two donors, which represent 38% of total revenue. During 2015, HARC received \$1,800,000 in contributions from one donor, which represents 25% of total revenue.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts reported as revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Recent financial accounting pronouncement – In August 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The amendments in this ASU are the first phase of changes aimed at providing more useful information to users of not-for-profit financial statements. Under this ASU, net assets will be presented in two classes: *net assets with donor restrictions* and *net assets without donor restrictions* and underwater endowments will be grouped with *net assets with donor restrictions*. New or enhanced disclosures will be required about the nature and composition of net assets, and the liquidity and availability of resources for general operating expenditures within one year of the balance sheet date. Expenses will be required to be presented by both nature and function and investment return will be presented net of external and direct internal investment expenses. Absent explicit donor stipulations, restrictions on long-lived assets will expire when assets are placed in service. The ASU is effective for fiscal periods beginning after December 15, 2017, but early adoption is permitted. Adoption of this ASU will impact the presentation and disclosures of the financial statements.

## NOTE 2 – PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	<u>2016</u>	<u>2015</u>
Land	\$ 829,376	\$ 829,376
Leasehold improvements	890,963	890,963
Furniture and equipment	694,352	1,054,973
Construction in progress	<u>5,258,199</u>	<u>718,530</u>
Total property and equipment, at cost	7,672,890	3,493,842
Accumulated depreciation	<u>(1,435,305)</u>	<u>(1,691,437)</u>
Property and equipment, net	<u>\$ 6,237,585</u>	<u>\$ 1,802,405</u>

### NOTE 3 – NOTES PAYABLE

Notes payable consist of the following:

	<u>2016</u>	<u>2015</u>
A \$4,500,000 line of credit with a bank maturing in September 2020 for the construction of a new building. The line bears an initial interest rate of LIBOR plus 1.6% (2.36% at December 31, 2016) and is adjusted to LIBOR plus 1.4% when the draw period ends in October 2017. The line of credit is secured by the new building. Principal and accrued interest are due monthly starting in October 2017.	\$ 1,569,748	
A \$1,500,000 unsecured line of credit agreement with the Endowment for Regional Sustainability Science (ERSS) with interest at LIBOR plus 0.50% (0.69% at December 31, 2016). Interest is payable quarterly and the line of credit expires on December 31, 2018.	<u>817,556</u>	<u>\$ 817,556</u>
Total notes payable	<u>\$ 2,387,304</u>	<u>\$ 817,556</u>

Notes payable are due as follows:

2017	\$ 837,179
2018	78,487
2019	78,487
2020	<u>1,393,151</u>
Total	<u>\$ 2,387,304</u>

HARC capitalized interest totaling approximately \$3,600 in 2016. Interest expense totaled approximately \$4,600 and \$6,700 in 2016 and 2015, respectively.

### NOTE 4 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	<u>2016</u>	<u>2015</u>
Capital projects	\$ 2,975,821	\$ 2,514,232
Development of Galveston Bay Report Card	222,544	435,412
Property Assessed Clean Energy program	43,160	
IFAS upgrades	41,468	44,720
Astrophysics Research	31,790	79,155
Internships	8,391	8,391
Environmentally Friendly Drilling Systems program	<u>4,892</u>	<u>48,607</u>
Total temporarily restricted net assets	<u>\$ 3,328,066</u>	<u>\$ 3,130,517</u>

## NOTE 5 – RESEARCH CONTRACTS AND GRANTS

Revenue from research contracts and grants includes the following:

	<u>2016</u>	<u>2015</u>
Federal government contracts and grants:		
U. S. Department of Energy	\$ 1,194,758	\$ 1,701,579
U. S. Department of the Interior	1,113,576	2,245,885
U. S. Environmental Protection Agency	191,606	319,405
U. S. Department of Commerce	<u>62,539</u>	<u>843</u>
Total federal government contracts and grants	<u>2,562,479</u>	<u>4,267,712</u>
State and local government contracts and grants:		
Texas Commission on Environmental Quality	30,864	120,699
Texas Parks and Wildlife	<u>1,686</u>	<u>          </u>
Total state and local government contracts and grants	<u>32,550</u>	<u>120,699</u>
Private research contracts and grants	<u>453,478</u>	<u>799,346</u>
Total research contracts and grants	<u>\$ 3,048,507</u>	<u>\$ 5,187,757</u>

HARC receives grants from federal, state and local government funding sources that require fulfillment of certain conditions as set forth in the related contracts and are subject to review and audit by the awarding agencies. Such reviews and audits could result in the discovery of unallowable activities and unallowable costs. Consequently, any of the funding sources may, at their discretion, request reimbursement for expenses or return of funds as a result of non-compliance by HARC with the terms of the contracts. Management believes such disallowances, if any, would not be material to HARC's financial position or changes in net assets.

## NOTE 6 – RELATED PARTY TRANSACTIONS

HARC subcontracted research services with the employers of certain members of the HARC Board of Directors totaling approximately \$21,000 and \$786,000 during 2016 and 2015, respectively. These subcontractors were obtained through a competitive award process or based on their technical qualifications.

## NOTE 7 – RETIREMENT PLAN

HARC has a tax-sheltered annuity plan (the Plan) established under §403(b) of the Internal Revenue Code. Under the terms of the Plan, HARC contributes a minimum of 5% of the participating employees' regular monthly salaries. In addition, HARC will match 1/2% for each percent the employee contributes up to 6%, for a maximum HARC contribution of 8% of regular salary. HARC contributed to the Plan approximately \$174,000 in 2016 and \$169,000 in 2015.

## NOTE 8 – SUBSEQUENT EVENTS

In July 2017, the \$1,500,000 line of credit from Note 3 was paid off.

Management has evaluated subsequent events through September 12, 2017, which is the date that the financial statements were available for issuance. As a result of this evaluation, no other events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.

## Houston Advanced Research Center

Schedule of Expenditures of Federal Awards for the year ended December 31, 2016

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<u>CLUSTER TITLE</u>					
<u>GRANTOR</u>			<u>Contract Number</u>		
<u>Pass-through Grantor</u>		<u>CFDA #</u>	<u>or Pass-through</u>	<u>Award</u>	<u>Federal</u>
<u>Program Title &amp; Period</u>			<u>Grantor Number</u>	<u>Amount</u>	<u>Expenditures</u>
RESEARCH AND DEVELOPMENT CLUSTER					
U. S. DEPARTMENT OF COMMERCE					
Passed through Texas General Land Office:					
Coastal Zone Management Administration					
Awards – Galveston Bay Mitigation					
#1	10/01/15 – 03/31/17	11.419	16-068-000-9112	\$100,000	<u>\$ 62,539</u>
Total U. S. Department of Commerce					<u>62,539</u>
U. S. DEPARTMENT OF THE INTERIOR					
Passed through Bureau of Land Management:					
Bureau of Land Management Training Workshops					
#2	10/01/16 – 03/31/17	15.XXX	L16PX02119	\$65,000	<u>17,238</u>
Passed through Harris County:					
Coastal Impact Assistance Program – Southeast Harris County					
Water Improvement Project					
#3	01/04/12 – 01/31/17	15.668	F12AP00071	\$592,825	159,564
Passed through Texas General Land Office:					
Coastal Impact Assistance Program – Coastal Impacts Technology Program					
#4	01/04/12 – 08/31/16	15.668	12-259-000-5595	\$3,998,244	<u>936,774</u>
Subtotal for 15.668					<u>1,096,338</u>
Total U. S. Department of the Interior					<u>1,113,576</u>
U. S. DEPARTMENT OF ENERGY					
Energy Efficiency and Renewable Energy Information Dissemination,					
Outreach, Training and Technical Analysis/Assistance – Southwest					
Combined Heat and Power Technical Assistance Partnerships					
#5	10/01/15 – 09/30/17	81.117	DE-EE0007233	\$825,000	<u>497,155</u>

(continued)

## Houston Advanced Research Center

Schedule of Expenditures of Federal Awards for the year ended December 31, 2016 *(continued)*

<u>CLUSTER TITLE</u>	<u>GRANTOR</u>		<u>Contract Number</u>			
<u>Pass-through Grantor</u>			<u>or Pass-through</u>		<u>Award</u>	<u>Federal</u>
<u>Program Title &amp; Period</u>	<u>CFDA #</u>		<u>Grantor Number</u>		<u>Amount</u>	<u>Expenditures</u>
RESEARCH AND DEVELOPMENT CLUSTER <i>(continued)</i>						
U. S. DEPARTMENT OF ENERGY <i>(continued)</i>						
Passed through State Energy Conservation Office:						
State Energy Program – Engaging Local Governments to Accelerate Energy Efficiency						
#6	10/31/15 – 08/31/16	81.041	15-0360		\$130,000	<u>94,099</u>
State Energy Program Special Projects – Texas Industrial Energy Efficiency and Combined Heat and Power						
#7	04/01/14 – 01/31/16	81.119	14-1531		\$100,000	5,029
State Energy Program Special Projects – Benchmarking Program						
#8	05/07/15 – 12/31/16	81.119	15-0232		\$275,000	<u>180,447</u>
Subtotal for 81.119						<u>185,476</u>
Passed through GSI Environmental, Inc.:						
Fossil Energy Research and Development – Advanced Analytical Methods for Air and Stray Gas Emissions						
#9	06/25/13 – 12/31/16	81.089	SC3875-005		\$38,200	15,273
Passed through GSI Environmental, Inc.:						
Fossil Energy Research and Development – Greenhouse Gases Emissions Factors for Compressors						
#10	10/17/16 – 09/30/17	81.089	SC4501-001		\$25,000	3,635
Fossil Energy Research and Development – Natural Gas Storage Emissions						
#11	10/17/16 – 09/30/17	81.089	SC4501-002		\$20,000	3,882
Passed through Research Partnership to Secure Energy for America:						
Fossil Energy Research and Development – Technology Integration Program Phase						
#12	07/03/12 – 07/02/16	81.089	10122-06		\$5,993,689	<u>395,238</u>
Subtotal for 81.089						<u>418,028</u>
Total U. S. Department of Energy						<u>1,194,758</u>

*(continued)*

## Houston Advanced Research Center

Schedule of Expenditures of Federal Awards for the year ended December 31, 2016 *(continued)*

<u>CLUSTER TITLE</u>				
<u>GRANTOR</u>				
<u>Pass-through Grantor</u>			<u>Contract Number</u>	
<u>Program Title &amp; Period</u>	<u>CFDA #</u>		<u>or Pass-through Grantor Number</u>	<u>Award Amount</u>
				<u>Federal Expenditures</u>
RESEARCH AND DEVELOPMENT CLUSTER <i>(continued)</i>				
U. S. ENVIRONMENTAL PROTECTION AGENCY				
Passed through Alabama-Coushatta Tribe of Texas:				
Surveys, Studies, Investigations, Demonstrations and Special Purpose				
Activities Relating to the Clean Air Act – Assessing Tribal Air Quality Exposure				
#13	02/22/16 – 11/08/16	66.034	ACT 2016	\$110,477
				<u>110,477</u>
Passed through Texas Commission on Environmental Quality:				
Galveston Bay Estuary Program – Assessing the Assimilative Capacity				
of Lake Livingston Reservoir and Related Impacts on Coastal Inflows				
#14	09/01/15 – 05/31/19	66.416	582-16-60126	\$160,000
				<u>33,873</u>
Passed through Texas State Soil and Water Conservation Board:				
Nonpoint Source Implementation Grants – Watershed Protection				
Planning – Double Bayou Watershed				
#15	04/01/12 – 08/31/16	66.460	11-08	\$1,023,614
				<u>47,256</u>
Total U. S. Environmental Protection Agency				<u>191,606</u>
TOTAL FEDERAL AWARDS/RESEARCH AND DEVELOPMENT CLUSTER				<u>\$ 2,562,479</u>

*See accompanying note to schedule of expenditures of federal awards.*

## Houston Advanced Research Center

Note to Schedule of Expenditures of Federal Awards for the year ended December 31, 2016

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### NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation – The schedule of expenditures of federal awards is prepared on the accrual basis of accounting. 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). Federal expenditures include allowable costs funded by federal grants. Allowable costs are subject to the cost principles of the Uniform Guidance and include both costs that are capitalized and costs that are recognized as expenses in HARC's financial statements in conformity with generally accepted accounting principles. Indirect costs are reported utilizing HARC's approved indirect cost rate from the United States Department of Interior and they do not utilize the 10% de minimus indirect rate.

Because the schedule presents only a selected portion of the operations of HARC, it is not intended to and does not present the financial position, changes in net assets, or cash flows of HARC.

Major programs – All of HARC's programs fall within the Research and Development cluster and, as such, are major programs.

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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 Board of Directors of  
Houston Advanced Research Center:

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 Houston Advanced Research Center (HARC), which comprise the consolidated statement of financial position as of December 31, 2016 and the related consolidated statements of activities and of cash flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated September 12, 2017.

***Internal Control Over Financial Reporting***

In planning and performing our audit of the financial statements, we considered HARC'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of HARC's internal control. Accordingly, we do not express an opinion on the effectiveness of HARC'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.

***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether HARC'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 result 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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Blazek & Vetterling*

September 12, 2017

**Independent Auditors' Report on Compliance for Each Major  
Program and Report on Internal Control Over  
Compliance Required by the Uniform Guidance**

To the Board of Directors of  
Houston Advanced Research Center:

**Report on Compliance for Each Major Federal Program**

We have audited Houston Advanced Research Center's (HARC) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of HARC's major federal programs for the year ended December 31, 2016. HARC'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 federal statutes, regulations, and the terms and conditions of its federal programs.

***Auditors' Responsibility***

Our responsibility is to express an opinion on compliance for each of HARC'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* 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 HARC'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 each major federal program. However, our audit does not provide a legal determination of HARC's compliance.

***Opinion on Each Major Federal Program***

In our opinion, HARC 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 December 31, 2016.

## Report on Internal Control Over Compliance

Management of HARC 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 HARC'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 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 HARC'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 a 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.



September 12, 2017

# Houston Advanced Research Center

Schedule of Findings and Questioned Costs for the year ended December 31, 2016

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## Section I – Summary of Auditors’ Results

### Financial Statements

Type of auditors’ report issued:  unmodified  qualified  adverse  disclaimer

Internal control over financial reporting:

- Material weakness(es) identified?  yes  no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)?  yes  none reported

Noncompliance material to the financial statements noted?  yes  no

### Federal Awards

Internal control over major programs:

- Material weakness(es) identified?  yes  no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)?  yes  none reported

Type of auditors’ report issued on compliance for major programs:  unmodified  qualified  adverse  disclaimer

Any audit findings disclosed that are required to be reported in accordance with 2 CFR §200.516(a)?  yes  no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
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Various	Research and Development
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Dollar threshold used to distinguish between Type A and Type B programs: \$750,000

Auditee qualified as a low-risk auditee?  yes  no

## Section II – Financial Statement Findings

There were no findings related to the financial statements which are required to be reported in accordance with *Government Auditing Standards*.

## Section III – Federal Award Findings and Questioned Costs

There were no findings for federal awards required to be reported in accordance with 2 CFR §200.516(a).