

**SOUTHWEST TRANSIT  
Eden Prairie, Minnesota**

**COMMUNICATIONS LETTER**

**Year Ended December 31, 2014**

**SOUTHWEST TRANSIT**

**TABLE OF CONTENTS**

<b>REPORT ON MATTERS IDENTIFIED AS A RESULT OF THE AUDIT OF THE FINANCIAL STATEMENTS .....</b>	<b>1</b>
<b>REQUIRED COMMUNICATION .....</b>	<b>2</b>
<b>FINANCIAL ANALYSIS.....</b>	<b>5</b>
<b>EMERGING ISSUES .....</b>	<b>11</b>



*Expert advice. When you need it.<sup>SM</sup>*

**REPORT ON MATTERS IDENTIFIED AS A RESULT OF  
THE AUDIT OF THE FINANCIAL STATEMENTS**

Board of Commissioners and Management  
SouthWest Transit  
Eden Prairie, Minnesota

In planning and performing our audit of the financial statements of SouthWest Transit (SWT), Eden Prairie, Minnesota, as of and for the year ended December 31, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered SWT's internal control over financial reporting (internal control) as a basis for designing auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SWT's internal control. Accordingly, we do not express an opinion on the effectiveness of SWT's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified.

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 SWT's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

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.

The accompanying memorandum also includes financial analysis provided as a basis for discussion. The matters discussed herein were considered by us during our audit and they do not modify the opinion expressed in our Independent Auditor's Report dated May 6, 2015, on such statements.

This communication is intended solely for the information and use of management, the Board of Commissioners, others within SWT and state oversight agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Kern, DeWenter, Viere, Ltd.*  
KERN, DEWENTER, VIERE, LTD.  
St. Cloud, Minnesota  
May 6, 2015

## **SOUTHWEST TRANSIT**

### **REQUIRED COMMUNICATION December 31, 2014**

We have audited the financial statements of SWT for the year ended December 31, 2014, and have issued our report thereon dated May 6, 2015. Professional standards require that we provide you with the following information related to our audit.

#### **OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA AND *GOVERNMENT AUDITING STANDARDS***

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of SWT. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of SWT's compliance with certain provisions of laws, regulations, contracts and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Our responsibility for the supplementary information accompanying the financial statements, as described by professional standards, is to evaluate the presentation of the supplementary information in relation to the financial statements as a whole and to report on whether the supplementary information is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

#### **PLANNED SCOPE AND TIMING OF THE AUDIT**

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit involved judgment about the number of transactions to be examined and the areas to be tested.

Our audit included obtaining an understanding of SWT and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets or (4) violations of laws or governmental regulations that are attributable to SWT or to acts by management or employees acting on behalf of SWT.

#### **QUALITATIVE ASPECTS OF ACCOUNTING PRACTICES**

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by SWT are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended December 31, 2014. We noted no transactions entered into by SWT during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the proper period.

**SOUTHWEST TRANSIT**  
**REQUIRED COMMUNICATION**  
**December 31, 2014**

**QUALITATIVE ASPECTS OF ACCOUNTING PRACTICES**

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was:

Depreciation – SWT is currently depreciating its capital assets over their estimated useful lives, as determined by management, using the straight-line method.

The financial statement disclosures are neutral, consistent and clear.

**DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT**

We encountered no significant difficulties in dealing with management in performing and completing our audit.

**CORRECTED AND UNCORRECTED MISSTATEMENTS**

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. We identified the following uncorrected misstatement of the financial statements. Management has determined its effect is immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

- OPEB liability related to GASB 45 is not recorded

In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

**DISAGREEMENTS WITH MANAGEMENT**

For purposes of this letter, a disagreement with management is a financial accounting, reporting or auditing matter, whether or not resolved to our satisfaction that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

**MANAGEMENT REPRESENTATIONS**

We requested certain representations from management that are included in the management representation letter.

**SOUTHWEST TRANSIT**  
**REQUIRED COMMUNICATION**  
**December 31, 2014**

**MANAGEMENT CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS**

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to SWT’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

**OTHER AUDIT FINDINGS OR ISSUES**

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as SWT’s auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

**OTHER MATTERS**

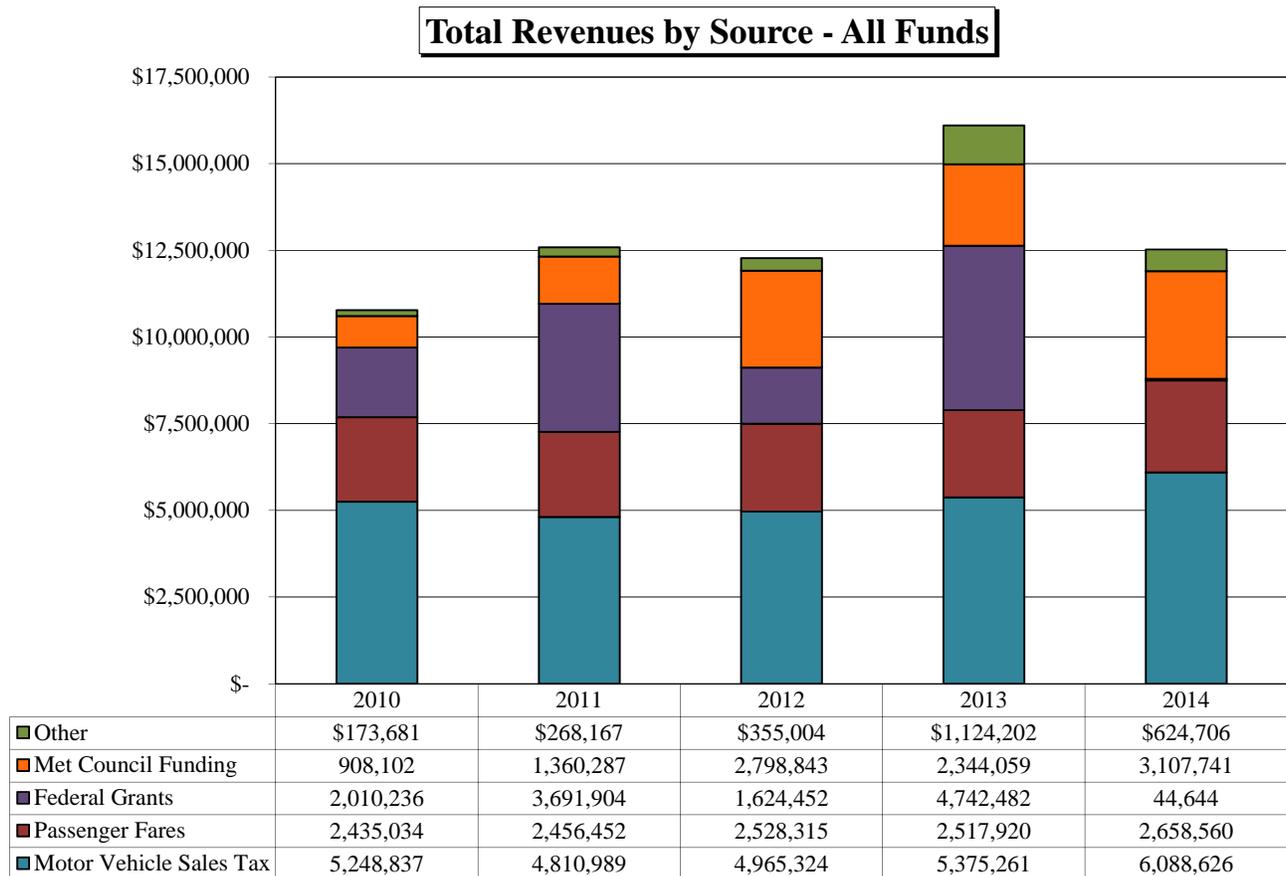
With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content and methods of preparing the information to determine that the information complies with accounting principles generally accepted in United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

## SOUTHWEST TRANSIT

### FINANCIAL ANALYSIS December 31, 2014

The following pages provide graphic representation of select data pertaining to the financial position and operations of SWT for the past five years. Our analysis of each graph is presented to provide a basis for discussion of past performance and how implementing certain changes may enhance future performance. We suggest you view each graph and document if our analysis is consistent with yours. A subsequent discussion of this information should be useful for planning purposes.

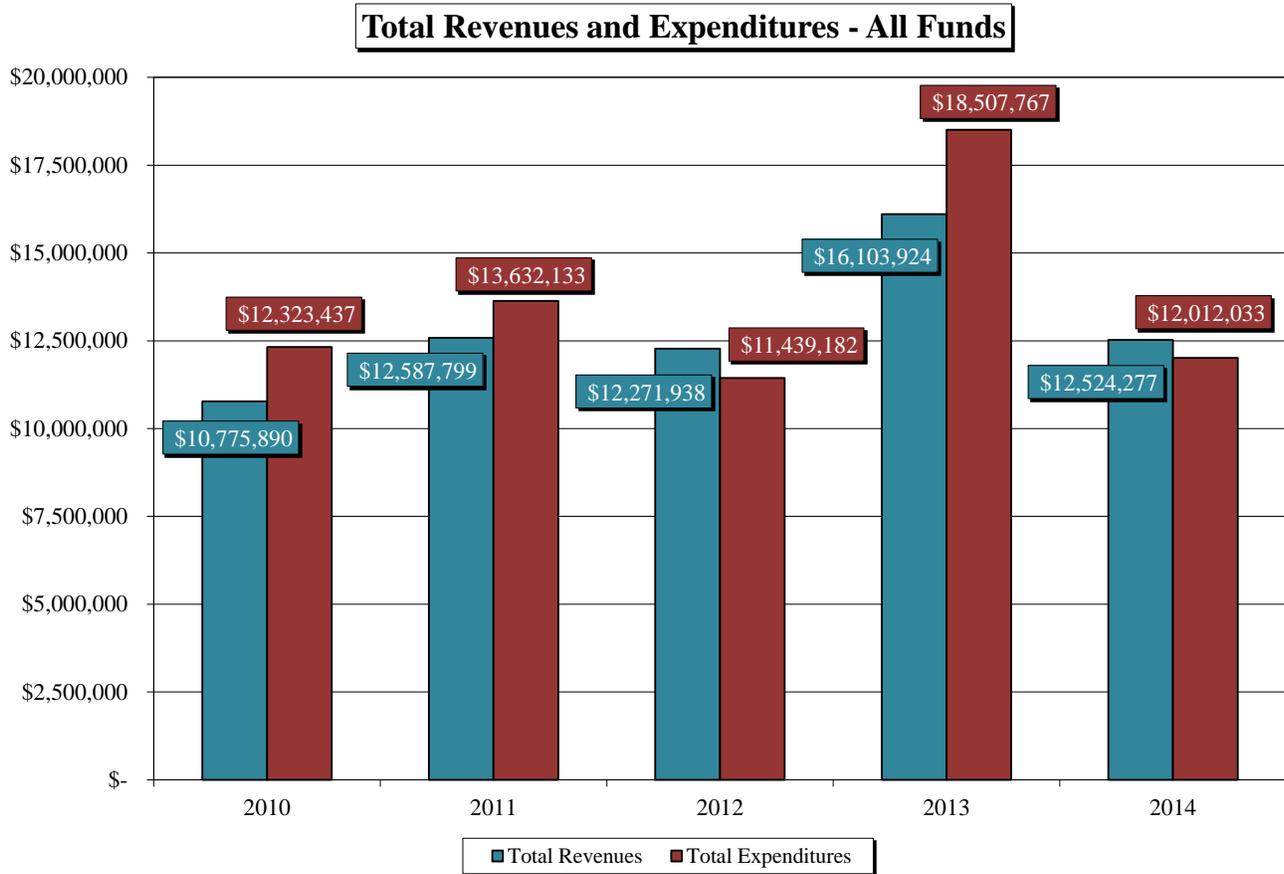
The following graphs are included to facilitate discussion of past operating results and related trends for future years' operations of SWT.



Revenue decreased \$ 3,579,647 in 2014 compared to 2013. Of this decrease, \$ 4,697,838 was due to a decrease in federal grant revenues that were related to the construction of the East Creek Station in 2013. Other revenues also decreased \$ 499,496 from 2013 due to the sale of land held for resale in the prior year. These decreases were offset by increases in Met Council Funding, passenger fares and motor vehicle sales tax. Met Council funding, which includes regionally allocated MYST, suburban transit provider appropriation, midlife bus rehabilitation grants and transit capital financial assistance grants, increased in 2014 by \$ 763,682, or 32.6%. This was due to an increase in the regionally allocated MVST, which is awarded in addition to MVST to maintain a fund balance at 35% of expenditures. Motor vehicle sales taxes received in 2014 increased \$ 713,365. Motor vehicle sales tax revenue is determined by a state allocation of vehicle sales tax in Minnesota and fluctuates each year based on vehicle sales in Minnesota. Passenger fares also increased in 2014, rising from \$ 2,517,920 in 2013 to \$ 2,658,560 in 2014, an increase of \$ 140,640. This was due to more service routes being offered in 2014 along with additional special events routes.

## SOUTHWEST TRANSIT

### FINANCIAL ANALYSIS December 31, 2014



Total expenditures exceeded total revenues in three of the last five years, which was by design to bring fund balance levels in line with Metropolitan Council's policies. In 2014, revenues exceeded expenditures by \$ 512,244. Total revenues decreased \$ 3,579,647, as mentioned on the previous page, while expenditures decreased \$ 6,495,734. This decrease in expenditures is primarily due to capital costs, which decreased \$ 6,195,365, which was mostly related to the construction of the East Creek Station and energy savings projects in 2013. In addition, debt service costs also decreased due to SWT refinancing the SouthWest Village debt in 2013, which was not done in 2014. This resulted in a decrease in debt service expenditures of \$ 1,961,853.

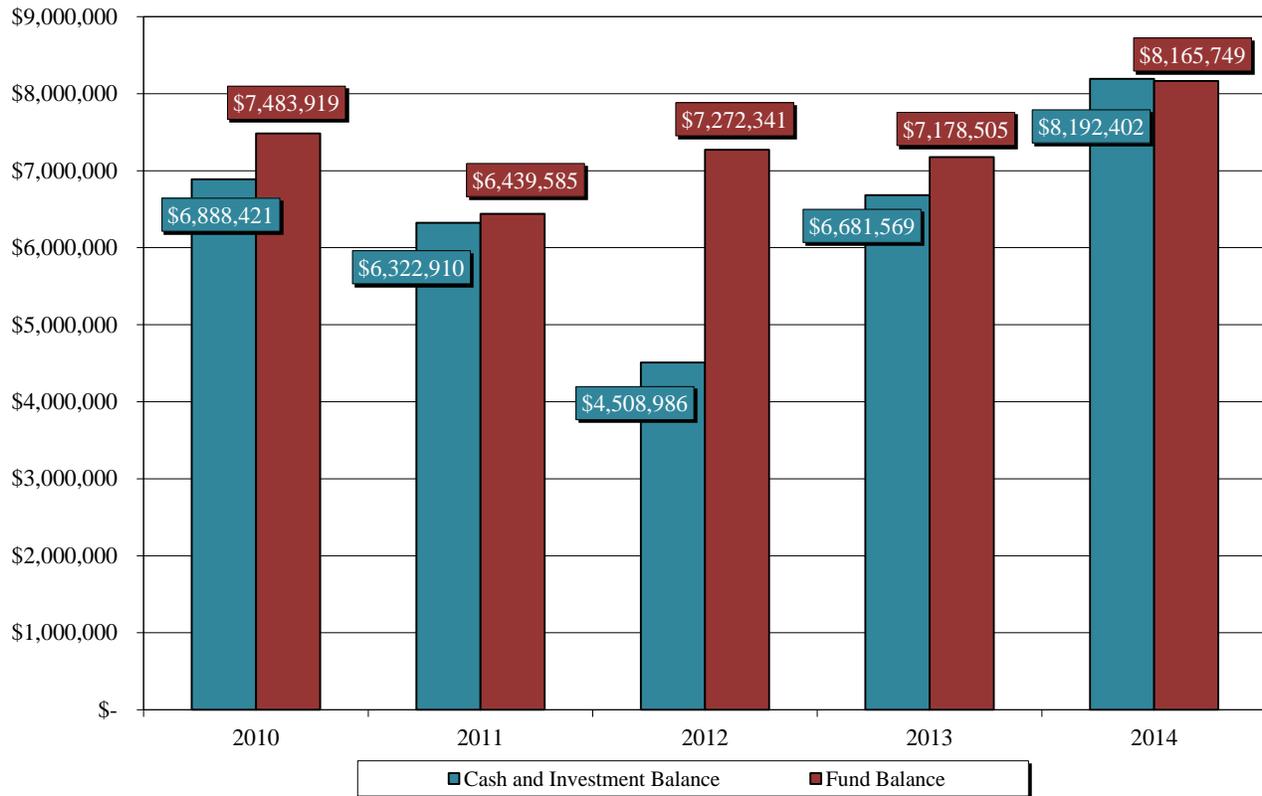
These decreases in expenditures, however, were partially offset by an increase in current expenditures of \$ 1,661,484. These increases are mostly due to costs related to additional operations mentioned above as SouthWest Transit added additional routes in 2014, including the leasing of a double deck bus. SouthWest Transit also spent more on building maintenance costs in 2014, increasing expenditures by \$ 467,305. Such costs include designing and replacing garage doors on all properties, general and preventative maintenance on the parking garages, costs associated with completing the East Creek Station project and fees relating to the sale of Chaska Garage.

# SOUTHWEST TRANSIT

## FINANCIAL ANALYSIS

December 31, 2014

**Cash and Fund Balance - All Funds**



The cash and investment balance was lower than fund balance in four of the five years presented. Cash and investments increased \$ 1,510,833 while fund balance increased \$ 987,244 from 2013 to 2014.

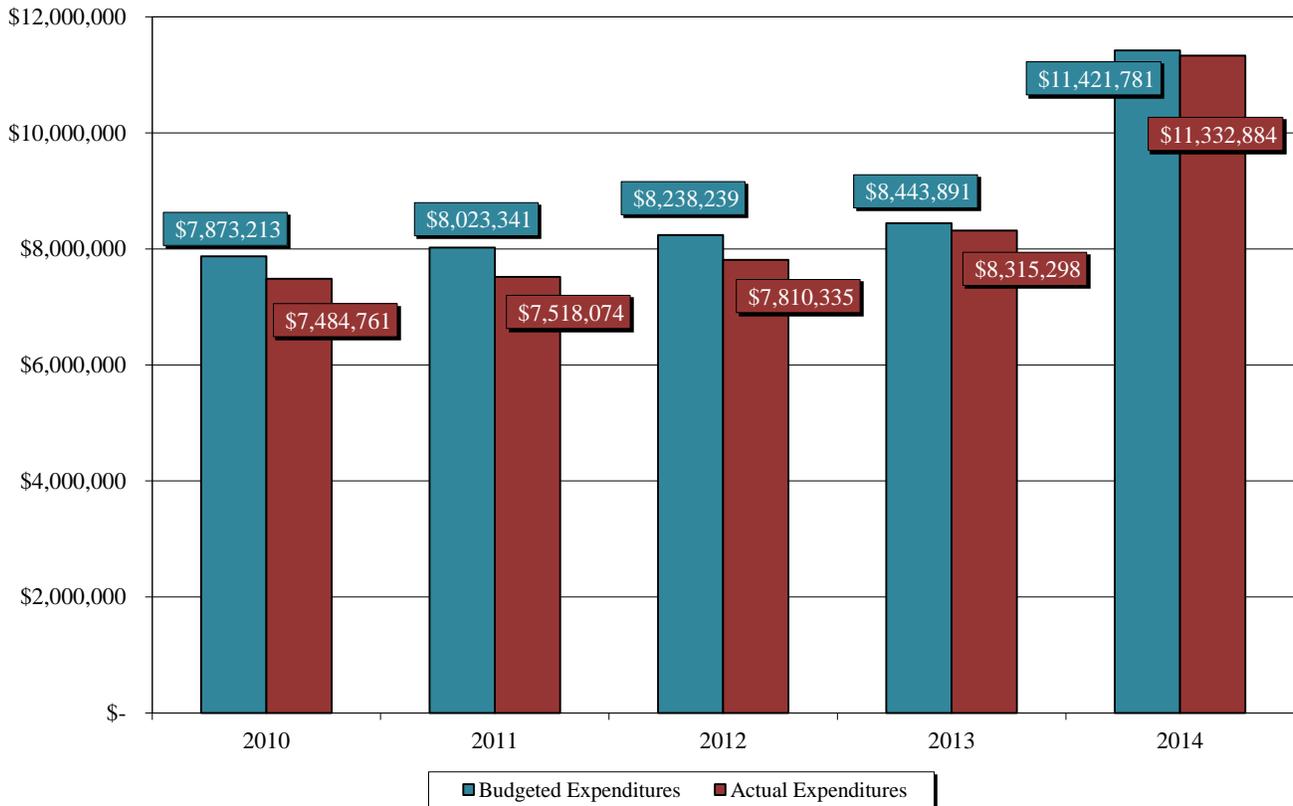
The cash and investment balance increased due to positive operations of \$ 987,243 and a decrease in intergovernmental receivables from the prior year of \$ 497,286. The decrease is due to the decrease in federal and state grant receivable related to the East Creek Station project.

The General Fund balance increased \$ 208,218 to \$ 3,438,527 in 2014 due revenues from operations and grants exceeding expenditures and transfers to other funds. The unassigned fund balance in the General Fund as of December 31, 2014 is \$ 2,893,152, which represents approximately 26%, or three months of expenditures, based on 2014 expenditure levels.

# SOUTHWEST TRANSIT

## FINANCIAL ANALYSIS December 31, 2014

**General Fund Expenditures - Budget to Actual**



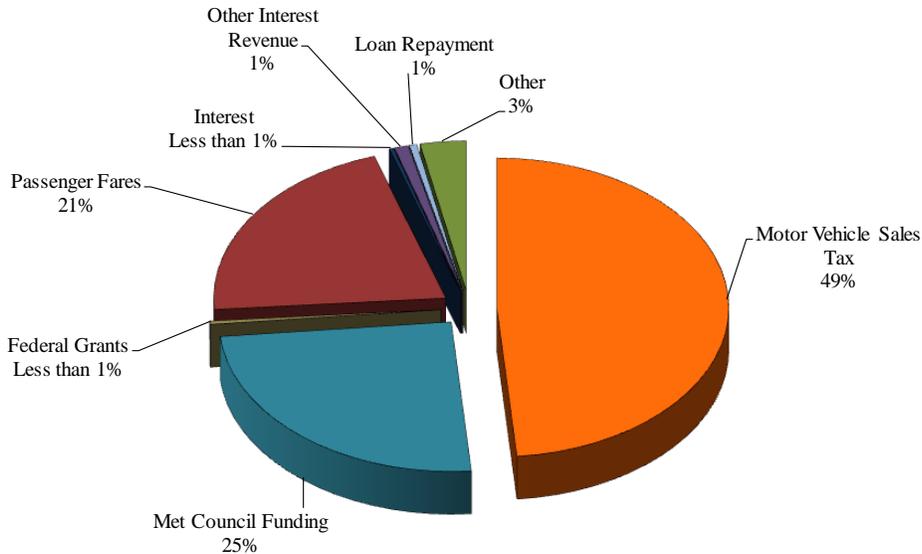
General Fund budgeted expenditures exceeded actual expenditures in all five years presented. Expenditures were under budget by \$ 88,897 in 2014. The largest variance was in general government expenditures, which were \$ 64,232 under budget. Expenditures in building and grounds and operations and vehicle maintenance were on budget in 2014, with variances of \$ 5,685 and \$ 18,980, respectively.

# SOUTHWEST TRANSIT

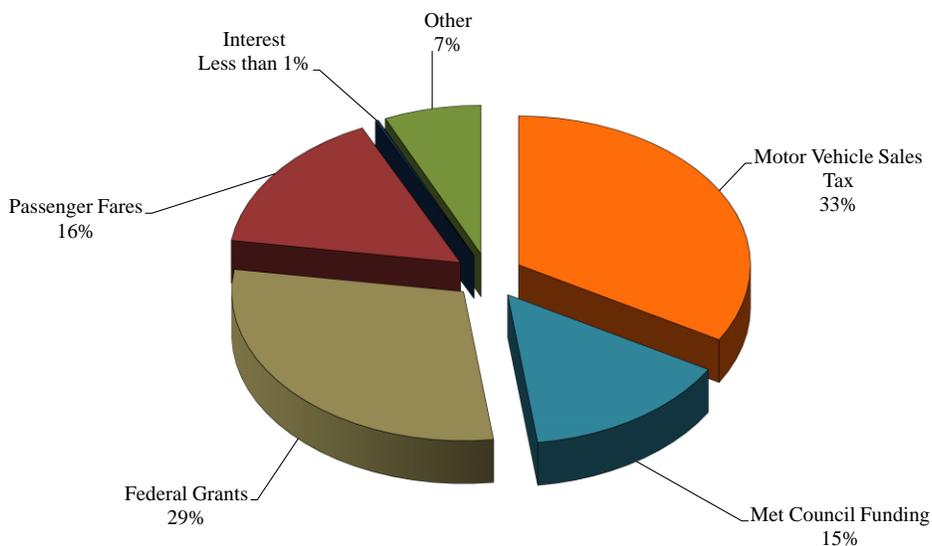
## FINANCIAL ANALYSIS December 31, 2014

The following pie charts show the allocation of revenue by source for all funds in 2014 and 2013. The most noticeable changes were in federal grants and motor vehicle sales tax. Other areas of revenue stayed consistent with the prior years.

**Operating Revenues by Source for 2014 - All Funds**



**Operating Revenues by Source for 2013 - All Funds**



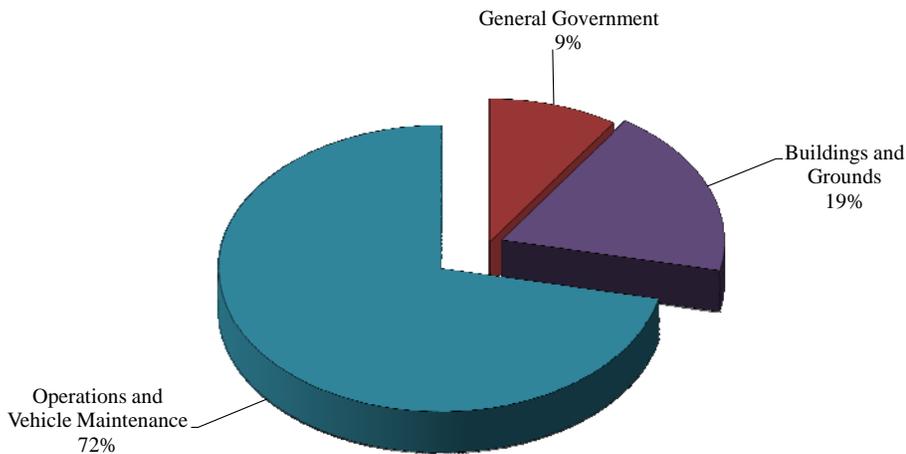
In the General Fund, the regional target for passenger fare revenue in relation to non capital expenditures is 28%. During 2014, SWT's passenger fare revenue as a percentage of non capital expenditures was 27%, while it was 30% in 2013.

# SOUTHWEST TRANSIT

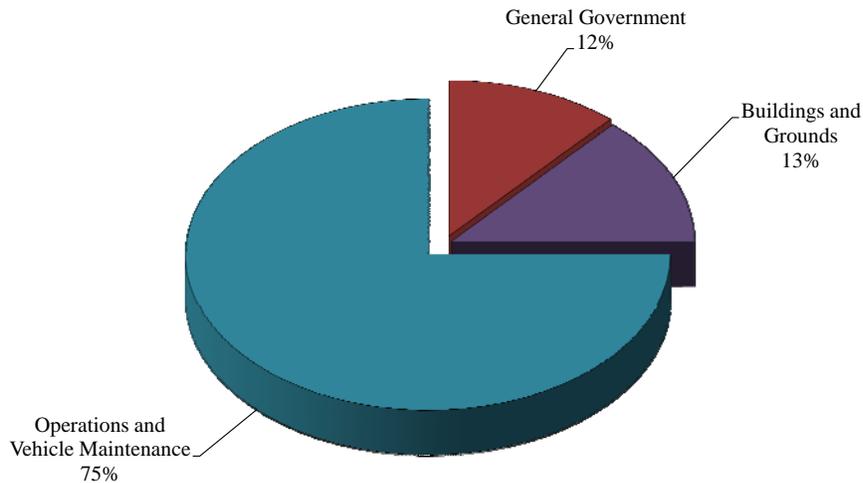
## FINANCIAL ANALYSIS December 31, 2014

The following pie charts show the allocation of expenditures by program for the General Fund in 2014 and 2013. The allocation change significantly in 2014 due to the capital costs of operations being moved to the General Fund at the request of the Metropolitan Council. As a result, general government and operations and vehicle maintenance expenditures as a percentage of total expenditures decreased while buildings and grounds increased.

**Operating Expenditures by Department for 2014  
General Fund**



**Operating Expenditures by Department for 2013  
General Fund**



## SOUTHWEST TRANSIT

### EMERGING ISSUES

December 31, 2014

#### Executive Summary

The following is an executive summary of financial and business related updates to assist you in staying current on emerging issues in accounting and finance. This summary will give you a preview of the new standards that have been recently issued and what is on the horizon for the near future. The most recent and significant updates include:

- **Internal Control Integrated Framework** – COSO has issued an updated integrated framework for internal control. The update is expected to make the integrated internal control framework easier to use and apply. In addition, the update takes into account globalization of businesses today and its interdependence on technology. The updated framework superseded the original framework beginning January 1, 2015.
- **Accounting Standard Update – Accounting for Pensions** – Governmental Accounting Standards Board (GASB) has issued new statements relating to accounting and disclosures for pension. The new statements require governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability. In addition, the statement includes new requirements for required supplementary information and more extensive footnote disclosures.
- **Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards** – The Office of Management and Budget (OMB) issued grant reform rules on December 23, 2013. This reform streamlines the language from eight existing OMB Circulars (listed below) into one consolidated set of guidance, in the code of Federal regulations, known as the “Super Circular”.

The following are extensive summaries of each of the current updates. As your continued business partner, we are committed to keeping you informed of new and emerging issues. We are happy to discuss these issues with you further and their applicability to your organization.

#### COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK

In 1992, the Committee on Sponsoring Organizations of the Treadway Commission (COSO) developed an internal control framework that has been adopted and used by entities worldwide. In 2013, COSO finalized and released an updated integrated internal control framework. The update is expected to make the integrated framework easier to use and apply. In addition, the update takes into account, the business environment of today and the reliance on and interdependence of technology within business systems.

The internal control update is not changing the core definition of internal control, the three categories of objectives or the five components of internal control.

COSO defines internal control as a process, affected by an entity’s board of directors, management and other personnel. This process is designed to provide reasonable assurance regarding the achievement of the three objectives, as follows: effectiveness and efficiency of operations; reliability of financial reporting; and compliance with applicable laws and regulations.

1. Internal control is a process. It is a means to an end, not an end in itself.
2. Internal control is not merely documented by policy manuals and forms. Rather, it is put in by people at every level of an organization.
3. Internal control can provide only reasonable assurance, not absolute assurance, to an entity’s management and board.
4. Internal control is geared to the achievement of objectives in one or more separate but overlapping categories.

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK (CONTINUED)**

The five components of internal control, which are unchanged, are as follows:

1. Control Environment – integrity, ethics, management style, etc.
2. Risk Assessment – identification and analysis of relevant risks
3. Control Activities – policies, procedures and activities, including segregation of duties
4. Information and Communication – ensure information effectively flows up, down and across the organization, both internally and externally
5. Monitoring Activities – assessment of the systems performance over time

The updated framework has changed to address the changes in business and operating environments, such as globalization of markets and operations, greater complexities in businesses, reliance on evolving technologies and expectations relating to preventing and detecting fraud. In addition, principles of effective internal controls have been added to each of the components of internal control as follows:

##### **Control Environment:**

1. Demonstrates a commitment to integrity and ethical values.
2. The board of directors is independent from management and exercises oversight responsibility of the performance of internal controls.
3. Management establishes structure, reporting lines, authority and responsibility.
4. Demonstrates a commitment to attract, develop and retain competent individuals.
5. Enforces accountability for individual's internal control responsibilities.

##### **Risk Assessment:**

1. Specifies suitable objectives with sufficient clarity.
2. Identifies and analyzes risk as a basis for how risks should be managed.
3. Assesses the potential for fraud risk.
4. Identifies and analyzes significant changes that could impact the system of internal controls.

##### **Control Activities:**

1. Selects and develops control activities that contribute to the mitigation of risks.
2. Selects and develops general controls over technology.
3. Deploys control activities through policies that establish what is expected and procedures that put policies into place.

##### **Information and Communication:**

1. Uses relevant information to support the functioning of other components of internal control.
2. Communicates information internally, including objectives and responsibilities necessary to support the internal controls.
3. Communicates with external parties regarding matters affecting internal control.

##### **Monitoring Activities:**

1. Conducts ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
2. Evaluates and communicates deficiencies to those parties responsible for corrective actions.

The updated framework also has additional examples relevant to operation, compliance and reporting objectives added.

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK (CONTINUED)**

While COSO integrated internal control framework is very extensive, this is only a short summary of some of the changes of the updated framework. The updated framework superseded the original framework beginning January 1, 2015.

#### **ACCOUNTING STANDARD UPDATE – ACCOUNTING FOR PENSIONS**

GASB Statement No. 68 replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement No. 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. GASB Statement No. 71 – *Pension Transition for Contributions Made Subsequent to the Measurement Date* – is an amendment of GASB No. 68.

- GASB 68 will require presentation of the local government’s proportionate share of the pension plan’s Net Pension Liability to be reported on the government-wide statement of net position and the proprietary fund statements of net position – based on last year’s employer contributions
- The Net Pension Liability is measured as the total pension liability less the amount of the pension plan’s fiduciary net position – PERA is currently estimating this around \$ 6-7 billion
- Governmental Funds will present pension expenditures equal to the total of 1) amounts paid by employer to the pension plan and 2) the change between the beginning and ending balances of amounts normally expected to be liquidated with expendable available financial resources (i.e. No Change)
- PERA has been proactive in steps toward implementation and the outlook for reporting to members appears good, based on current plans – the hope is that most of the implementation will be a “plug-in” of PERA generated data
- PERA has a June 30 fiscal year-end – this is the measurement date you will utilize for your presentation in your December 31 financial statements six months subsequent to that date
- Other Deferred Inflows/Outflows will include: differences between expected and actual economic experience and investment earnings, changes in assumptions and changes in employer proportion and difference between contributions and proportionate share of pension expense
- Required Supplementary Information will be two separate schedules – Schedule of Changes in Net Pension Liability and Related Ratios & Schedule of Contributions – 10-year presentation for each with notes
- GASB 71 clarifies that in the year of implementation you must determine the deferred outflows associated with pension contributions made subsequent to the measurement date – even if it is not practical to determine the other deferred inflows and outflows

#### **PERA Plan:**

- Perform annual actuarial valuations to determine funded status and liabilities
- Require plan actuary to calculate collective amount of items requiring deferred treatment
- Engage external auditor or audit actuarial census data and schedule of employer’s proportionate share
- Communicate results to the local governments
- Provide RSI and suggested footnotes

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **ACCOUNTING STANDARD UPDATE – ACCOUNTING FOR PENSIONS (CONTINUED)**

##### **Local Impacts:**

- Your organization’s proportionate share of the plan’s net pension liability will be recognized as a liability on your organization’s government-wide statements. As of December 31, 2014, PERA has estimated the liability for your organization to be \$ 1,141,492, based on the total unfunded liability as of their June 30, 2014 year end.
- Expenditures will continue to be tracked in the fund statements for your statutory contributions, but a reconciling item will be needed to adjust these contributions with your government-wide expenses which will be represented by the change in the net pension liability
- As a result, your financial statements/financial position will be immediately impacted by funding shortfalls at the pension plan
- Additional RSI presenting 10 years of information regarding net pension liability, required & actual contributions and related ratios
- Adds more extensive note disclosures, including sensitivity analysis of investment return assumption
- Requires employer to track annual balances of deferred outflows of resources and inflows of resources.
- Must describe signification assumptions and other inputs used to measure total pension liability.

#### **UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES AND AUDIT REQUIREMENTS FOR FEDERAL AWARDS**

The Office of Management and Budget (OMB) issued grant reform rules on December 23, 2013. This uniform grant guidance streamlines Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards.

##### **Effective Dates**

Federal agencies must implement the requirements to be effective by December 26, 2014. Non-federal entities will need to implement the new Administrative Requirements and Cost Principles for all new Federal Awards made after December 26, 2014. Audit Requirements are effective for fiscal years beginning on or after December 26, 2014.

##### **Objective of OMB Grant Reform**

This reform streamlines the language from eight existing OMB Circulars into one consolidated set of guidance, in the code of Federal regulations, known as the “Super Circular”. The objective of the grant reform is to reduce administrative burden for non-federal entities receiving Federal Awards while reducing the risk of waste, fraud and abuse by:

1. Eliminating duplicative and conflicting guidance
2. Focusing on performance over compliance for accountability
3. Encouraging efficient use of information technology and shared services
4. Providing for consistent and transparent treatment of costs
5. Limiting allowable costs to make the best use of federal resources
6. Setting standard processes using data definitions
7. Encouraging non-federal entities to have family friendly policies
8. Strengthening oversight
9. Targeting audit requirements on risk of waste, fraud and abuse

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES AND AUDIT REQUIREMENTS FOR FEDERAL AWARDS (CONTINUED)**

This grant reform complements targeted efforts by OMB and a number of Federal agencies to reform overall approaches to grant-making by implementing innovative, outcome-focused grant making decisions and processes in collaboration with their non-federal partners.

#### **Administrative Requirements – Subpart A-D of Federal Register**

Following are some of the notable items in the updated Administrative Requirements.

- Must is defined as required
- Should is defined as best practice or recommended approach
- The term “vendor” is no longer used and was replaced with the term “contractor” (Section 200.23)
- Personally Identifiable Information (PII) and Protected Personally Identifiable Information (PPII) are defined (Sections 200.79 and 200.82)
- Fixed amount awards focused on meeting performance milestones (Section 200.201)
- Emphasis on performance goals and performance reporting (Section 200.301)
- Defined that computers are considered supplies, not equipment (Section 200.940)
- Flexibility in electronic documentation retention, with associated internal controls (Section 200.335)

#### **Internal Controls (Section 200.303)**

Internal controls should comply with:

- “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States and the “Internal Control Integrated Framework” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)
- Federal statutes, regulations and terms and conditions of the Federal award

Internal controls must:

- Evaluate and monitor compliance
- Take prompt action for noncompliance
- Take reasonable measures to safeguard PPII and other sensitive information

#### **Procurement Standards (Sections 200.317 through 200.326)**

Guidelines provide five different procurement methods

- Micro-purchases
- Small purchases
- Sealed bids
- Competitive proposals
- Noncompetitive proposals

Entities must have a documented procurement policy, written standards of conduct covering organizational conflicts of interest and must maintain oversight to ensure that contractors perform in accordance with the terms, conditions and specifications of their contracts or purchase orders.

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES AND AUDIT REQUIREMENTS FOR FEDERAL AWARDS (CONTINUED)**

##### **Subrecipient Monitoring (Sections 200.330 through 200.332 and 200.521)**

The pass-through entity must clearly identify the agreements as a subaward and must provide up to 13 different award identification pieces of information within the contract. There are also other required disclosures described for all requirements imposed by the pass-through entity on the subrecipient, indirect cost rate, allowing access to records, etc. An evaluation of each subrecipients risk of noncompliance is also required.

##### **Cost Principles – Subpart E of Federal Register**

Following are some of the notable items in the updated Cost Principles.

##### **Indirect/Direct Costs (Sections 200.413-200.414)**

- Salaries of administrative or clerical staff could be directly charged to a federal program if they meet certain conditions.
- Any non-federal entity that has never negotiated an indirect cost rate may elect to charge a de minimis rate of 10% of modified total direct costs which may be used indefinitely
- Federally negotiated indirect cost rates must be accepted by all federal awarding agencies (usually).
- Any non-federal entity that has a federally negotiated indirect cost rate may apply for a one-time extension of a current negotiated indirect cost rates for a period of up to four years.

##### **Time and Effort Reporting (Section 200.430)**

Charges to Federal Awards must be based on records that accurately reflect the work performed.

- Records are to be supported by a system of internal controls which provides reasonable assurance that the charges are accurate, allowable and properly allocated
- There is flexibility in process used to meet those standards
- Personnel activity reports not specifically required
- Maintained budget estimates may be used for interim accounting purposes, provided that, the non-federal entity's system of internal controls includes processes to review after-the-fact interim charges made to a Federal Award based on budget estimates to ensure adjustments are made so final amounts to Federal Awards are proper.

##### **Audit Requirements – Subpart F of Federal Register**

Following are some of the notable items in the updated Audit Requirements.

- Single Audit threshold raised from \$ 500,000 in Federal Awards per year to \$ 750,000 in Federal awards per year
- Major program determination changes include:
  - Type A/B program threshold is a sliding scale with a minimum of \$ 750,000
  - Percentage of coverage rule changes to 40% (50% currently) for non-low risk auditees and 20% (25% currently) for low risk auditees
- Updated criteria for a low-risk auditee
  - Going concern is incorporated
  - Cognizant/oversight agency can no longer waive exception
- Reporting for questioned costs threshold raised from \$ 10,000 to \$ 25,000

## **SOUTHWEST TRANSIT**

### **EMERGING ISSUES**

**December 31, 2014**

#### **UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES AND AUDIT REQUIREMENTS FOR FEDERAL AWARDS (CONTINUED)**

##### **Other Items of Interest**

- List of items requiring prior written approval (*Section 200.407*)
- Advertising and public relations clarified, include program outreach (*Section 200.421*)
- Conference spending clarified (*Section 200.432*)
- Employee “morale” costs eliminated (*Section 200.437*)

##### **Example of Strategy to Implement OMB Grant Reform Changes**

1. Understand grant reform changes
2. Assign an internal expert who will be responsible for leading effort (time, resources and availability)
3. Establish a team and include those in program, financial and budget sides of federal grant management
4. Develop a plan and concentrate on areas of most significance first
5. Obtain approval from management and those charged with governance as it relates to policy changes
6. Attain/Provide training on new requirements and new entity specific policies and procedures
7. Monitor plan and focus on areas of most significant change

##### **Additional Resources on OMB Grant Reform**

- OMB Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards
  - (<https://www.federalregister.gov/articles/2013/12/26/2013-30465/uniform-administrative-requirements-cost-principles-and-audit-requirements-for-federal-awards>)
- COFAR FAQs
  - (<https://cfo.gov/wp-content/uploads/2013/01/2-C.F.R.-200-FAQs-2-12-2014.pdf>)
  - (<https://cfo.gov/wp-content/uploads/2014/08/2014-08-29-Frequently-Asked-Questions.pdf>)
- OMB Policy Statements
  - ([http://www.whitehouse.gov/OMB/grants\\_docs](http://www.whitehouse.gov/OMB/grants_docs))