Southwest Transit
Eden Prairie, Minnesota

Communications Letter

December 31, 2016

bergan KDV
CPAS | ADVISORS

Southwest Transit
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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 governmental activities, each major fund, and the aggregate remaining fund information of SouthWest Transit (SWT), Eden Prairie, Minnesota, as of and for the year ended December 31, 2016, 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 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 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. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls.

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 April 18, 2017, on such statements.

BerganKDV, Ltd.
bergankdv.com

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.

Bergan KDV, Ltd.

St. Cloud, Minnesota
April 18, 2017

SouthWest Transit
Required Communication

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of SWT as of and for the year ended December 31, 2016. 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 opinions 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.

Generally accepted accounting principles provide for certain required supplementary information (RSI) to supplement the basic financial statements. Our responsibility with respect to the RSI, which supplements the basic audit financial statements, is to apply certain limited procedures in accordance with generally accepted auditing standards. However, the RSI was not audited and, because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance, we do not express an opinion or provide any assurance on the RSI.

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.

Our responsibility with respect to the other information in documents containing the audited financial statements and auditor's report does not extend beyond the financial information identified in the report. We have no responsibility for determining whether this other information is properly stated. This other information was not audited and we do not express an opinion or provide any assurance on it.

SouthWest Transit
Required Communication

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 the notes to financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended December 31, 2016. 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.

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 estimates affecting the financial statements were:

> Depreciation – SWT is currently depreciating its capital assets over their estimated useful lives, as determined by management, using the straight-line method.
>
> Net Pension Liability, Deferred Outflows of Resources Related to Pensions, and Deferred Inflows of Resources Related to Pensions – These balances are based on an allocation by the pension plans using estimates based on contributions.

We evaluated the key factors and assumptions used to develop the accounting estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

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.

SouthWest Transit
Required Communication

CORRECTED AND UNCORRECTED MISSTATEMENTS

Professional standards require us to accumulate all known and likely 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.

MANAGEMENT CONSULTATIONS WITH OTHER 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.

SouthWest Transit
Required Communication

OTHER MATTERS

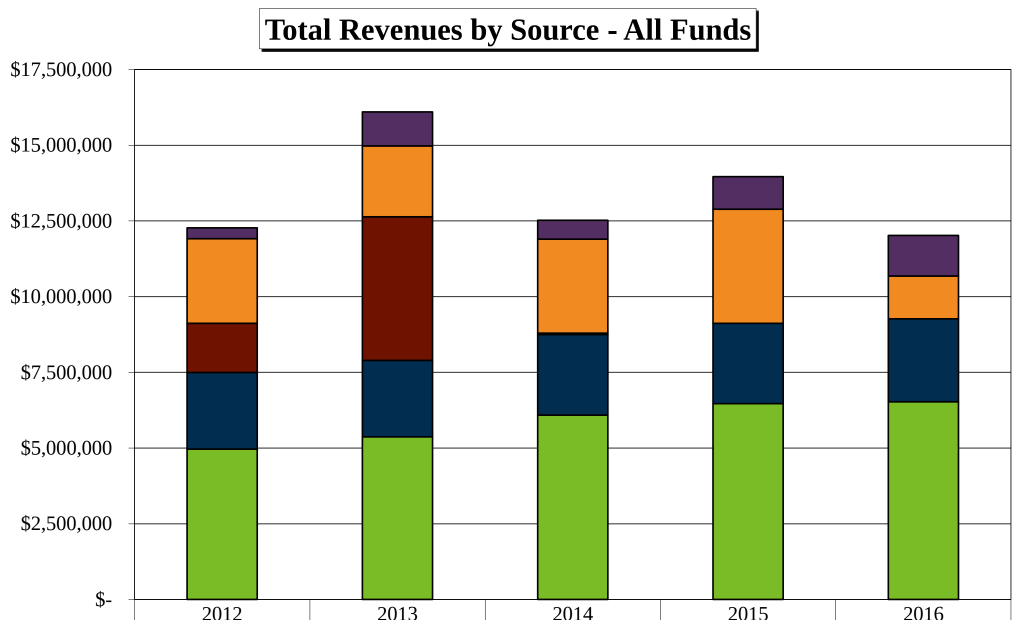
We applied certain limited procedures to the RSI that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

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 the 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.

We were not engaged to report on the other information accompanying the financial statements, but are not RSI. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

SouthWest Transit
Financial Analysis

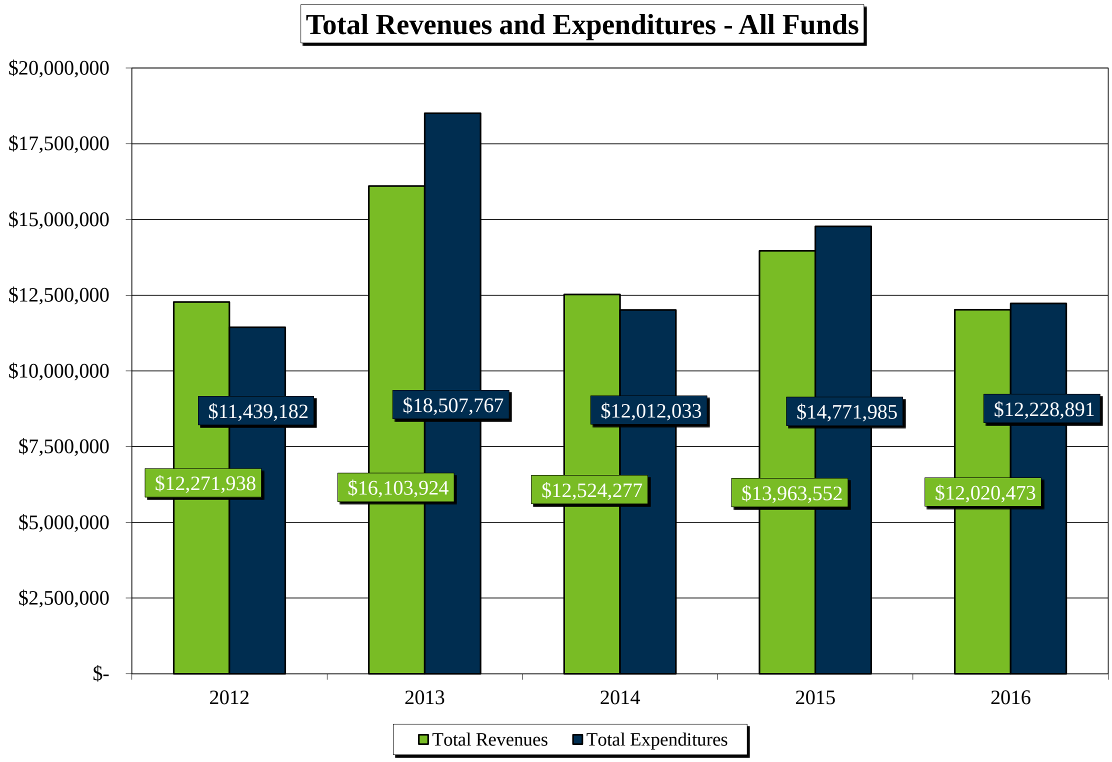
The following pages provide graphic representation of select data pertaining to the financial position and operations of SWT for the past five years. The graphs are included to facilitate discussion of past operating results and related trends for future years' operations of SWT. Our analysis of each 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.



	2012	2013	2014	2015	2016
Other	$355,004	$1,124,202	$624,706	$1,077,626	$1,338,492
Met Council Funding	2,798,843	2,344,059	3,107,741	3,766,156	1,410,910
Federal Grants	1,624,452	4,742,482	44,644	-	-
Passenger Fares	2,528,315	2,517,920	2,658,560	2,653,727	2,745,131
Motor Vehicle Sales Tax	4,965,324	5,375,261	6,088,626	6,466,043	6,525,940

Revenue decreased $1,943,079 in 2016 compared to 2015. All of this decrease was due to a decrease of $2,355,246 in Met Council funding, which includes regionally allocated MVST, suburban transit provider appropriation, midlife bus rehabilitation grants, and transit capital financial assistance grants. The regionally allocated MVST decreased $1,644,000 as a result of Met Council reducing SWT's grant amount to keep SWT's fund balance in the 35-40% maximum allowance range, as set by Met Council. The decrease was also related to funding SWT received in 2015 to purchase two 30 foot buses. This decrease in revenue was offset by increases in passenger fares and other revenues. Passenger fares revenue increased $91,404 as a result of SW Prime operating for a full year in 2016, compared to a partial year in 2015. Other revenues increased $260,866 from 2015 due to an increase of approximately $100,000 in the insurance dividend received, an increase of $60,000 in the contract with the City of Plymouth related to Plymouth MetroLink, a new fuel rebate of approximately $50,000 in 2016, and a new suburb to suburb grant in 2016 that totaled approximately $81,000. These increases to other revenues were offset slightly by a decrease in revenue from the City of Carver related to service in Carver as a result of some service being cut due to low ridership. Motor vehicle sales taxes received in 2016 increased $59,897. 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.

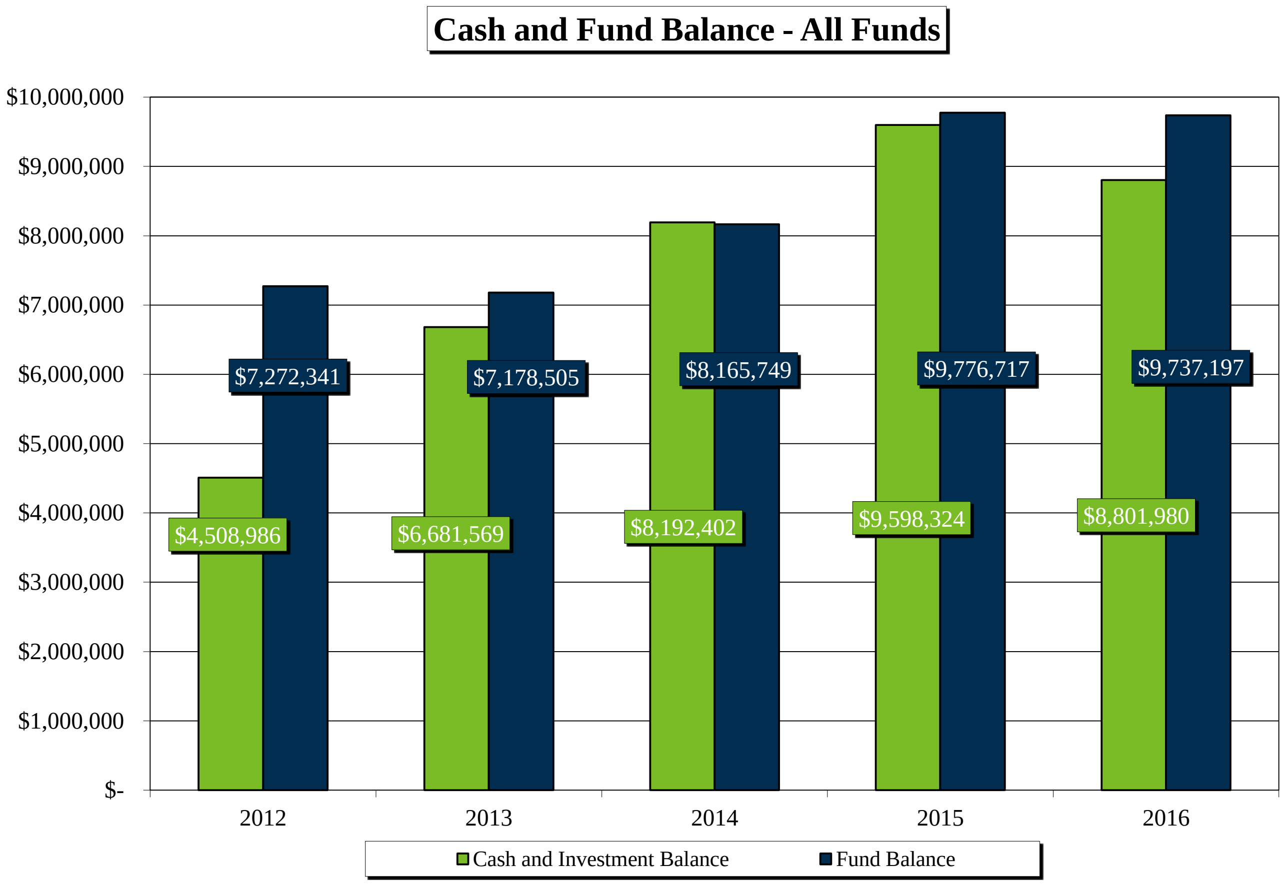
SouthWest Transit
Financial Analysis



Total expenditures exceeded total revenues in three of the last five years, which was by design to bring fund balance levels in line with Met Council's policies. In 2016 expenditures exceeded revenues by $208,418. Total revenues decreased $1,943,079, as mentioned on the previous page, while expenditures decreased $2,543,094. This decrease in expenditures is primarily due to capital costs, which decreased $3,473,296, and was mostly related to the construction of the Eden Prairie garage remodel project in 2015. There were also other larger projects in 2015 that did not occur in 2016 including canopy painting, ramp repairs, erosion control, a new bus lease for a turtle top bus, and a significant bus rehabilitation grant. In addition, debt service costs also increased due to SWT entering a new lease-purchase agreement in 2015 to finance the Eden Prairie garage remodel project. This resulted in principal and interest payments due in 2016 being higher than what was due in 2015 by approximately $150,000.

These decreases in capital expenditures were partially offset by an increase in current expenditures of $779,857. General government current expenditures increased $223,892 as a result of implementing a new website in 2016, additional radio advertising, a new marketing service professional fee and marketing position that was added in 2016, and wage increases. Buildings and grounds current expenditures increased $262,550 from 2015 as a result of the need to replace a security system after a lightning strike and new preventative maintenance activity in 2016 which typically does not occur every year. Operations and vehicle maintenance current expenditures increased $293,415 as a result of SWT employing a full-time assistant planner for all of 2016, an increase in temporary drivers related to special event routes, increase in software costs related to the new SW Prime service being active for the full year (Ridecell), a new contract with First Transit in 2016 that included an increase in fees, and an increase in insurance costs due to having five additional SW prime buses to insure compared to the prior year. These increases were offset by decreases in motor fuel and lubricants as a result in a decrease in the average fuel price from $2.33 per gallon in 2015 to $1.63 per gallon in 2016 and a decrease in equipment leases related to the double deck bus.

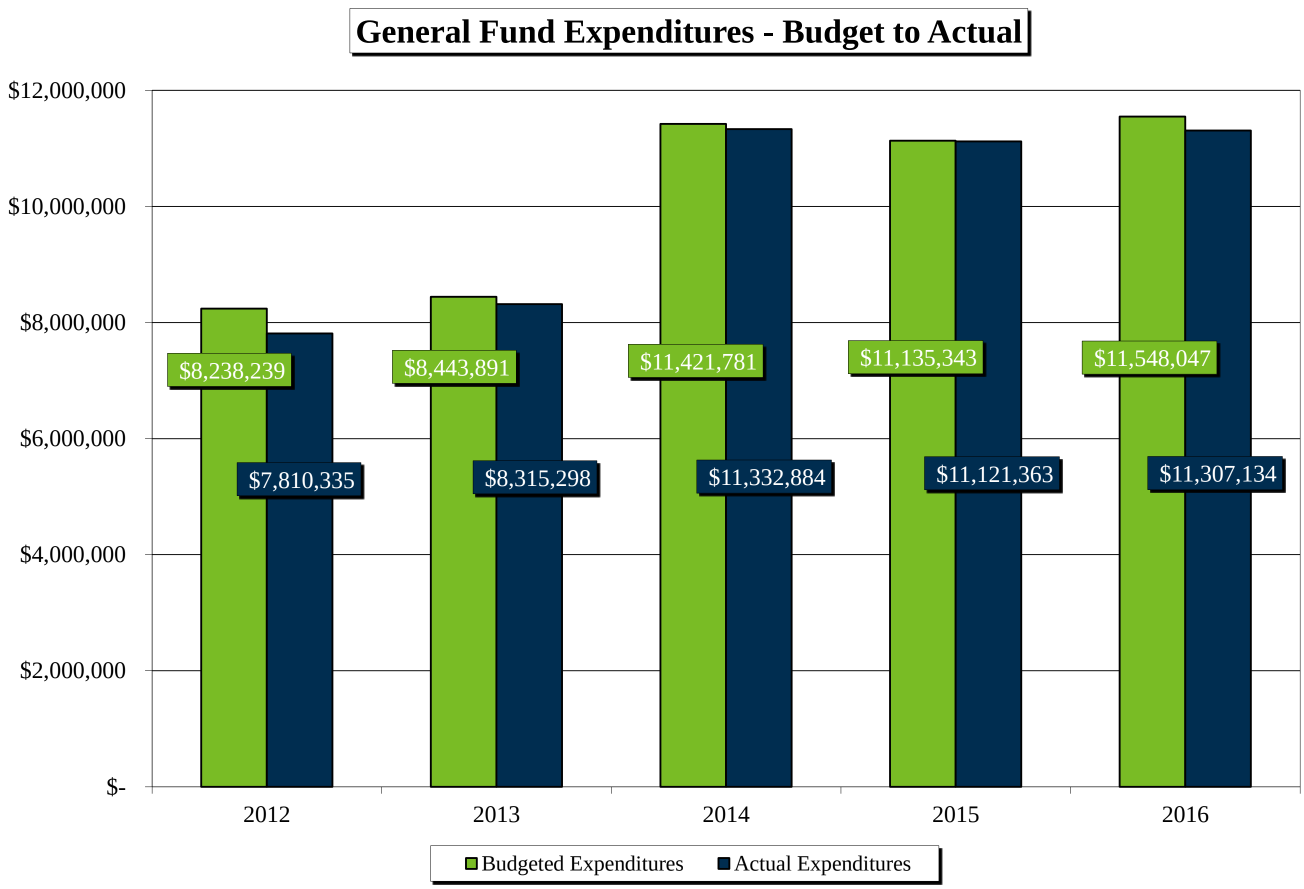
SouthWest Transit
Financial Analysis



The cash and investment balance was lower than fund balance in four of the five years presented. Cash and investments decreased $796,344 while fund balance decreased $39,520 from 2015 to 2016.

The cash and investment balance decreased due to negative overall operations of $39,520, an overall increase in inventory and land held for resale of $573,728, and a decrease in accounts, contracts, retainage, and salaries payable from the prior year of $238,970.

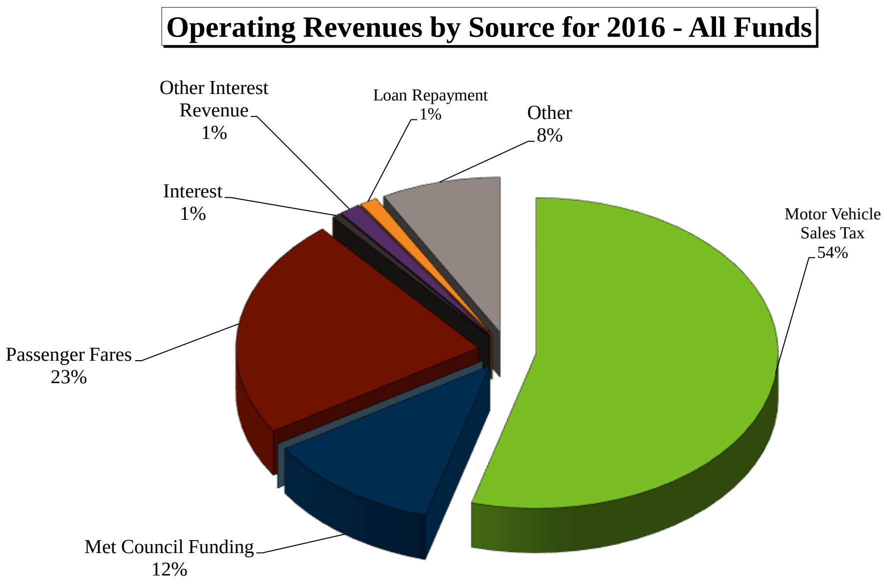
The General Fund balance decreased $50,282 to $4,661,886 in 2016 due to revenues from operations and grants coming in under expenditures and transfers to other funds. The unassigned fund balance in the General Fund as of December 31, 2016, is $4,043,568, which represents approximately 36%, or 4 months of expenditures, based on 2016 expenditure levels.

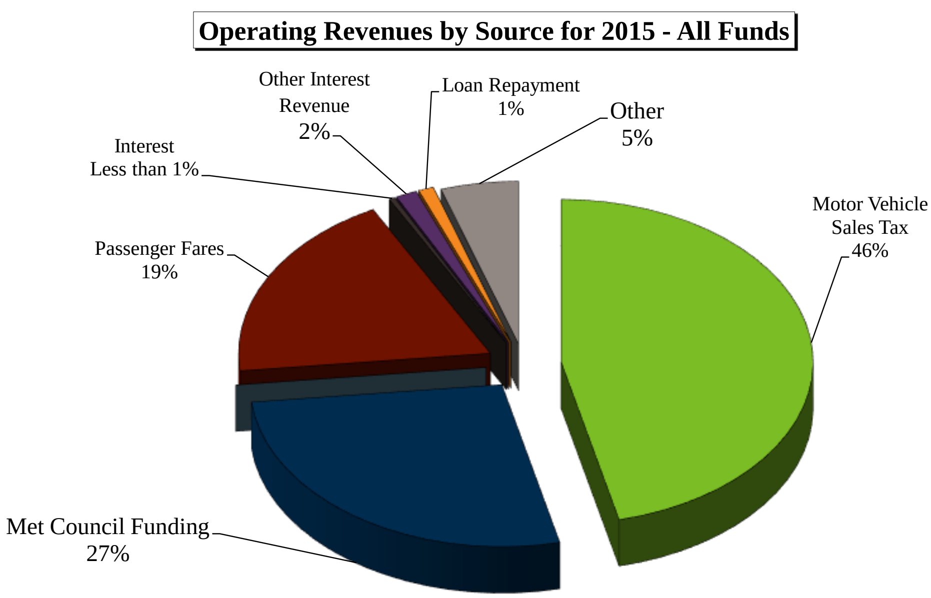


General Fund budgeted expenditures exceeded actual expenditures in all five years presented. Expenditures were under budget by $240,913 in 2016. The largest variance was in operations and vehicle maintenance current expenditures, which were $167,710 under budget. This budget variance is the result of the software maintenance contract coming in approximately $77,000 under budget as a result of budgeting for SWT's proportionate share of Met Council's AVL software while not incurring the expenditure, vehicle body shop repair expenditures coming in approximately $26,000 less than anticipated as a result of budgeting based off of 2015 actual results and having less repairs needed in 2016, as well as several other line items coming in under budget as well. The other more significant variance was in operations and vehicle maintenance capital outlay expenditures, which were $103,689 under budget. This is the result of the capital costs of operating coming in under budget due to the annunciator project coming in lower than anticipated. Expenditures in the other programs were relatively consistent with budgeted amounts.

SouthWest Transit
Financial Analysis

The following pie charts show the allocation of revenue by source for all funds in 2016 and 2015. There were significant changes between 2015 and 2016 as a result of the significant decrease in Met Council funding in 2016. As a result, the allocation of revenue by source increased for most revenue sources.



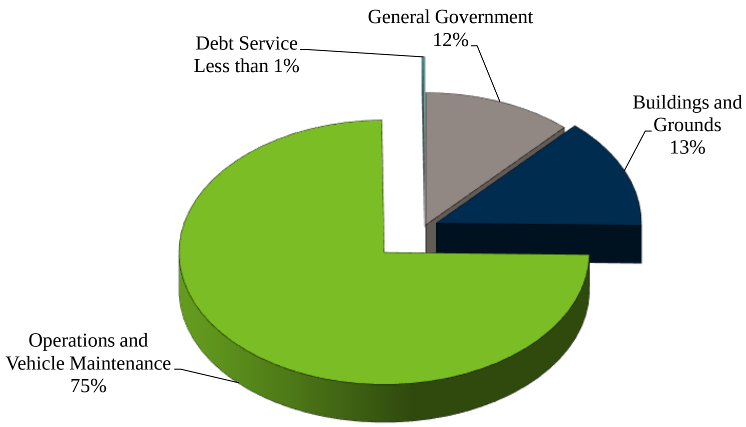


In the General Fund, the regional target for passenger farebox recovery revenue percentage in relation to operating expenditures is 28%. During 2016, SWT's passenger fare revenue as a percentage of operating expenditures was 29.57%, while it was 28.34% in 2015.

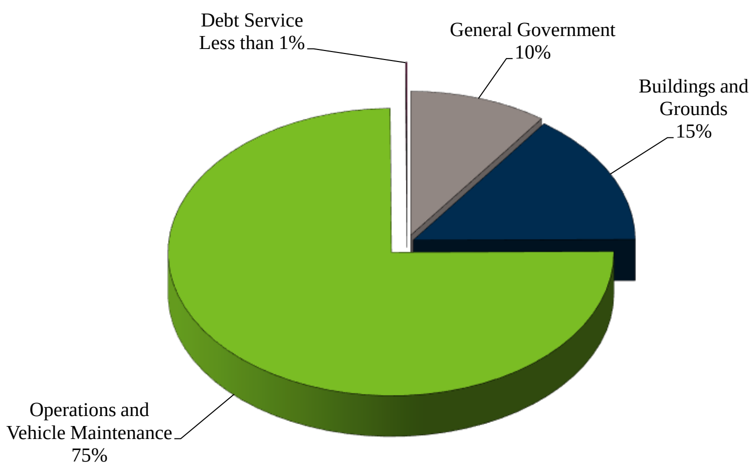
SouthWest Transit
Financial Analysis

The following pie charts show the allocation of expenditures by program for the General Fund in 2016 and 2015. The allocation changed slightly in 2016 due to the increases in general government, operations and vehicle maintenance, and buildings and grounds expenditures as discussed earlier.

Operating Expenditures by Department for 2016 - General Fund



Operating Expenditures by Department for 2015 - General Fund



SouthWest Transit
Emerging Issue

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:

- **Accounting Standard Update – GASB Statement No. 75 – Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions** – GASB has issued GASB Statement No. 75 relating to accounting and financial reporting for postemployment benefits other than pensions. The new statement requires governments in all types of OPEB plans to present more extensive note disclosures and required supplementary information (RSI) about their OPEB liabilities.

The following is an extensive summary of each the current update. 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.

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 75 – *ACCOUNTING AND FINANCIAL REPORTING FOR POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS*

The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

This Statement replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, for OPEB. Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, establishes new accounting and financial reporting requirements for OPEB plans.

GASB Statement No. 75 requires governments to report a liability on the face of the financial statements for the OPEB that they provide:

- Governments that are responsible only for OPEB liabilities related to their own employees and that provide OPEB through a defined benefit OPEB plan administered through a trust that meets specified criteria will report a *net OPEB liability*—the difference between the total OPEB liability and assets accumulated in the trust and restricted to making benefit payments.

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 75 – *ACCOUNTING AND FINANCIAL REPORTING FOR POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS* (CONTINUED)

- Governments that participate in a cost-sharing OPEB plan that is administered through a trust that meets the specified criteria will report a liability equal to their *proportionate share of the collective OPEB liability* for all entities participating in the cost-sharing plan.

- Governments that do not provide OPEB through a trust that meets specified criteria will report the *total OPEB liability* related to their employees.

GASB Statement No. 75 carries forward from Statement No. 45 the option to use a specified alternative measurement method in place of an actuarial valuation for purposes of determining the total OPEB liability for benefits provided through OPEB plans in which there are fewer than 100 plan members (active and inactive). This option was retained in order to reduce costs for smaller governments.

GASB Statement No. 75 requires governments in all types of OPEB plans to present more extensive note disclosures and required supplementary information (RSI) about their OPEB liabilities. Among the new note disclosures is a description of the effect on the reported OPEB liability of using a discount rate and a healthcare cost trend rate that are one percentage point higher and one percentage point lower than assumed by the government. The new RSI includes a schedule showing the causes of increases and decreases in the OPEB liability and a schedule comparing a government's actual OPEB contributions to its contribution requirements.

Information provided above was obtained from www.gasb.org.