Southwest Transit
Eden Prairie, Minnesota

Communications Letter

December 31, 2018

bergankdv

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 financial statements 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, 2018, 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 have not been 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 over financial reporting, 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. A reasonable possibility exists when the likelihood of an event occurring is either reasonably possible or probable as defined as follows: reasonably possible – the chance of the future event or events occurring is more than remote but less than likely; probable – the future event or events are likely to occur. 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 8, 2019, 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.

Bergan KDV, Ltd.

St. Cloud, Minnesota
May 8, 2019

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, 2018. Professional standards require that we advise you of the following matters related to our audit.

OUR RESPONSIBILITY IN RELATION TO THE FINANCIAL STATEMENT AUDIT

As communicated in our engagement letter, our responsibility, as described by professional standards, is to form and express opinions about whether the financial statements prepared by management with your oversight are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of its respective 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 audited 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.

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.

PLANNED SCOPE AND TIMING OF THE AUDIT (CONTINUED)

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.

COMPLIANCE WITH ALL ETHICS REQUIREMENTS REGARDING INDEPENDENCE

The engagement team, others in our firm, as appropriate, our firm, and our network firms have complied with all relevant ethical requirements regarding independence.

QUALITATIVE ASPECTS OF SIGNIFICANT ACCOUNTING PRACTICES

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by SWT is included in the notes to financial statements. There have been no initial selection of accounting policies and no changes to significant accounting policies or their application during 2018. 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.
>
> Total Other Post Employment Benefits (OPEB) Liability, Deferred Outflows of Resources Related to OPEB and Deferred Inflows of Resources Related to OPEB – These balances are based on an actuarial study using the estimates of future obligations of SWT for post employment benefits.

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.

SouthWest Transit
Required Communication

SIGNIFICANT DIFFICULTIES ENCOUNTERED DURING THE AUDIT

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

UNCORRECTED AND CORRECTED 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. Further, professional standards require us to also communicate the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole. We identified the following uncorrected misstatements 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.

- Earnest money on a pending land sale became nonrefundable; the amount is in unearned revenue rather than recognizing revenue in 2018

DISAGREEMENTS WITH MANAGEMENT

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter, which could be significant to SWT's financial statements or the auditor's report. No such disagreements arose during the course of the audit.

REPRESENTATIONS REQUESTED FROM MANAGEMENT

We requested certain written representations from management, which are included in the management representation letter.

MANAGEMENT'S CONSULTATIONS WITH OTHER ACCOUNTANTS

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management has informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

OTHER SIGNIFICANT MATTERS, FINDINGS, OR ISSUES

In the normal course of our professional association with SWT, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, operating conditions affecting SWT, and operating plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as SWT's auditors.

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.

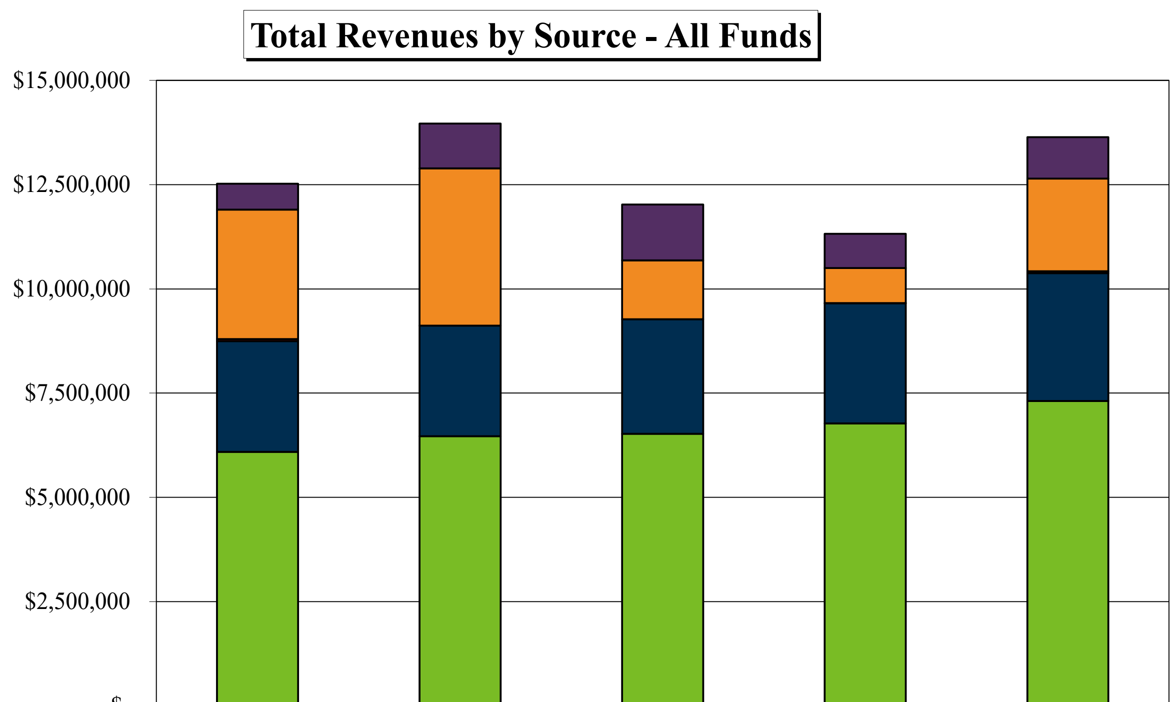
With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United 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.

TOTAL REVENUES BY SOURCE – ALL FUNDS



	2014	2015	2016	2017	2018
Other	$624,706	$1,077,626	$1,338,492	$817,418	$992,883
Met Council Funding	3,107,741	3,766,156	1,410,910	837,166	2,220,141
Federal Grants	44,644	-	-	6,588	49,650
Passenger Fares	2,658,560	2,653,727	2,745,131	2,882,098	3,065,441
Motor Vehicle Sales Tax	6,088,626	6,466,043	6,525,940	6,772,950	7,309,568

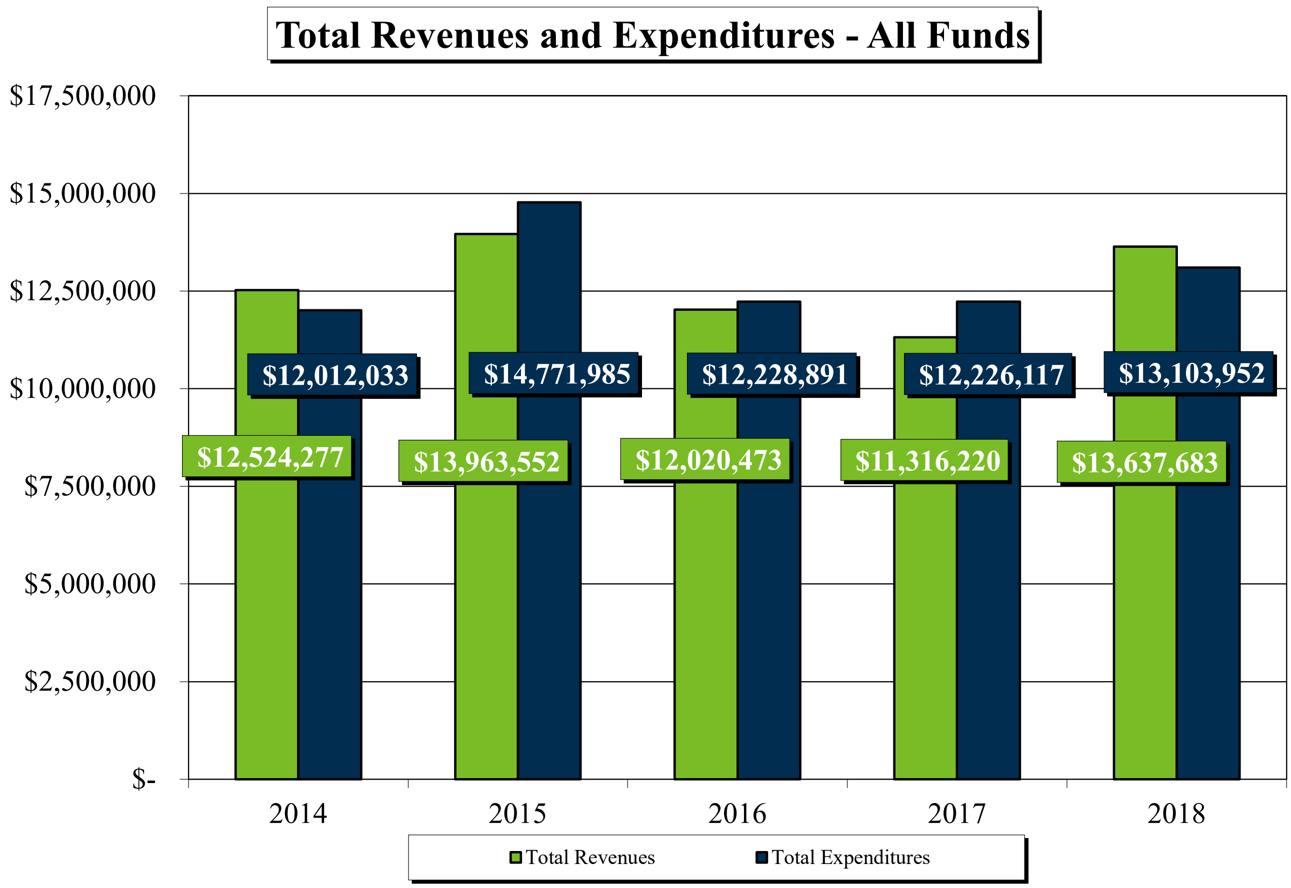
TOTAL REVENUES BY SOURCE – ALL FUNDS (CONTINUED)

Revenue increased $2,321,463 in 2018 compared to 2017.

- Met Council revenue increased $1,382,975
  - Regionally allocated MVST increased $990,620 as a result of SWT receiving the full amount allocated to them in 2018 while Met Council reduced the amount in 2017 to keep SWT's fund balance in the 25-35% maximum allowance range, as set by Met Council
  - SWT received an approximately $76,000 grant for an East Creek Station generator
  - SWT received a new state appropriation in 2018 in the amount of approximately $406,000
  - SWT received approximately $55,000 in 2018 for bus wash improvements
  - The previous increases were offset by a decrease related to approximately $118,000 received in 2017 related to legal fees associated with the sale of SWT's building
- Motor vehicle sales tax increased $536,618
  - This 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 increased $183,343 as a result of transit wide increase in fares, an increase in the fare for the state fair routes, and an increase in SW Prime ridership
- Other revenue increased $175,465 due to increases in advertising revenues and suburb to suburb grant funding

SouthWest Transit
Financial Analysis

TOTAL REVENUES AND EXPENDITURES – ALL FUNDS

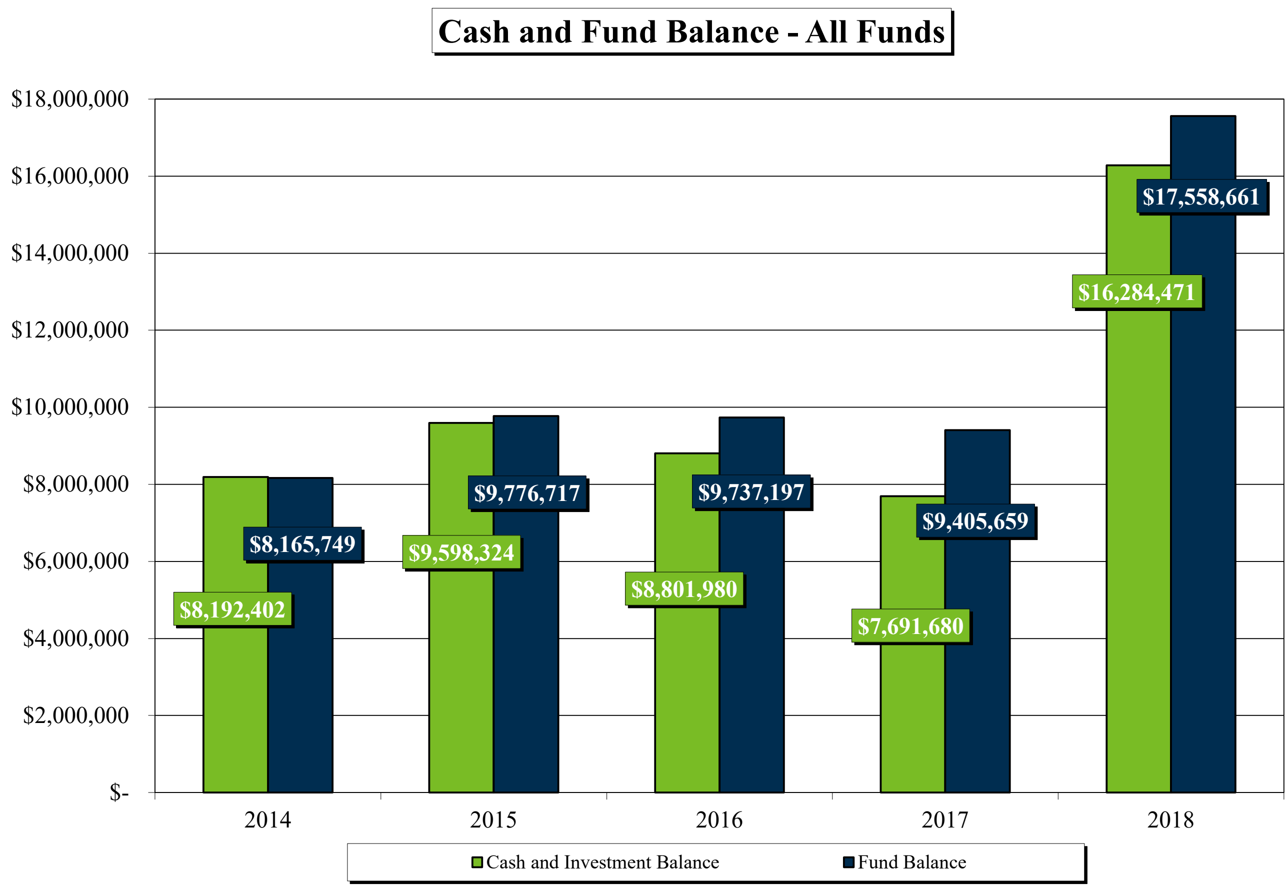


Total expenditures exceeded total revenues in three of the last five years, which was by design to bring fund balance levels in line with Met Council's policies. In 2018, revenues exceeded expenditures by $533,731. Total revenues increased $2,321,463, as mentioned on the previous page, while expenditures increased $877,835. There were some changes in expenditures by program:

- General government current expenditures increased $140,370
  - Result of full-time accounting technician position being in place for 2018
  - Increase in legal fees
  - Increase in costs associated with advertising and marketing
- Operations and vehicle maintenance current expenditures increased $552,911
  - Fees related to the contract with First Transit increased due to an increase in Prime service demands
  - Motor fuel and lubricants increased due to increased usage
  - Adjustments for the write off of obsolete parts was made in 2018
  - Increased software maintenance contract costs
- Buildings and grounds capital outlay expenditures increased $121,691
  - Primarily the result of construction at the Eden Prairie garage related to the relocation of offices

SouthWest Transit
Financial Analysis

CASH AND FUND BALANCE – ALL FUNDS

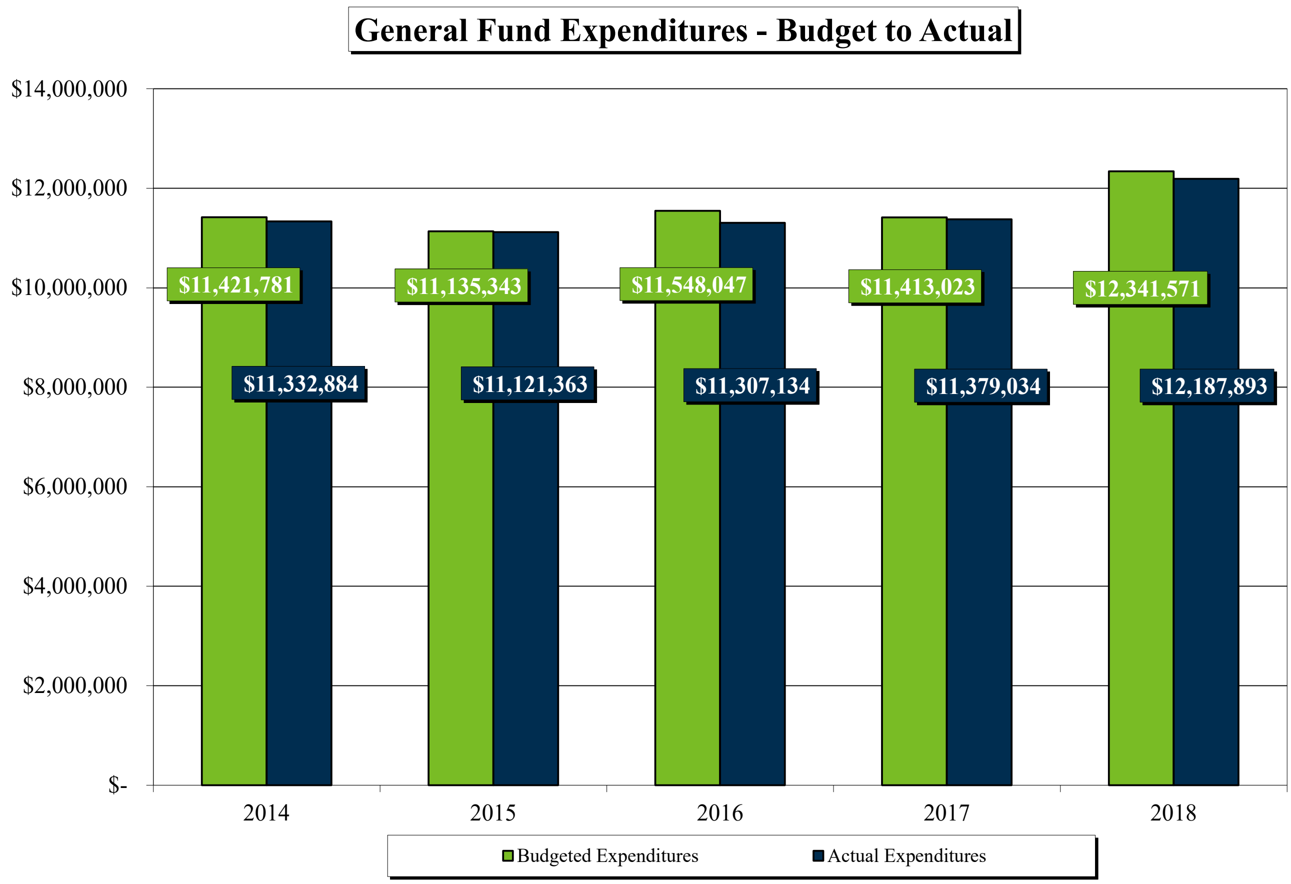


The cash and investment balance was lower than fund balance in four of the five years presented. Cash and investments increased $8,592,791 while fund balance increased $8,153,002 from 2017 to 2018.

The cash and investment balance increased significantly due to the property sale of the SouthWest Station and an overall decrease in receivables of $352,103, offset by a decrease in accounts, contracts, and salaries payable from the prior year of $144,052.

The General Fund balance increased $707,540 to $4,290,610 in 2018 due to revenues from operations and grants coming in over expenditures and transfers to other funds. This was primarily the result of an increase in regionally allocated MVST. The unassigned fund balance in the General Fund as of December 31, 2018, is $3,827,438, which represents approximately 33%, or 4 months of expenditures, based on 2018 budgeted operating expenditure levels.

GENERAL FUND EXPENDITURES – BUDGET TO ACTUAL



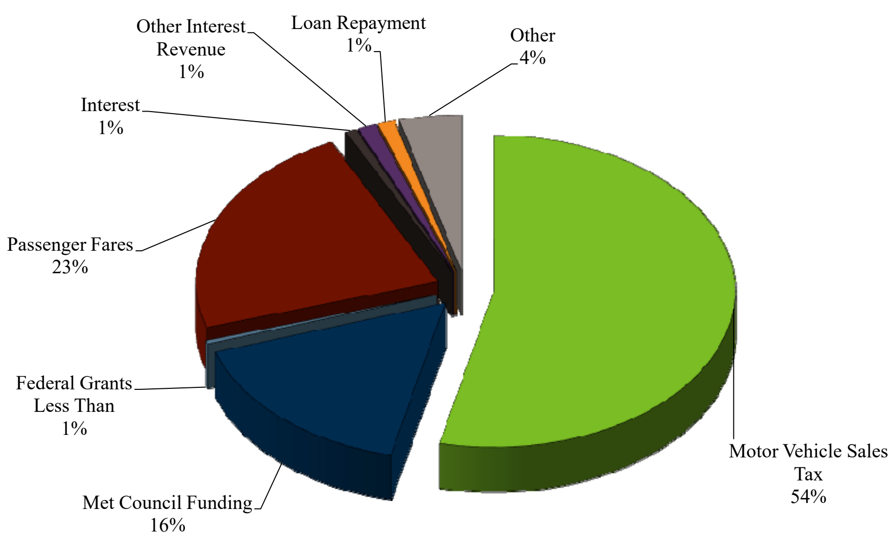
General Fund budgeted expenditures exceeded actual expenditures in all five years presented. Expenditures were under budget by $153,678 in 2018. The largest variance was in operations and vehicle maintenance capital expenditures, which were $66,941 under budget. Buildings and grounds capital expenditures were $47,810 under budget. All other expenditures were relatively consistent with budgeted amounts.

SouthWest Transit
Financial Analysis

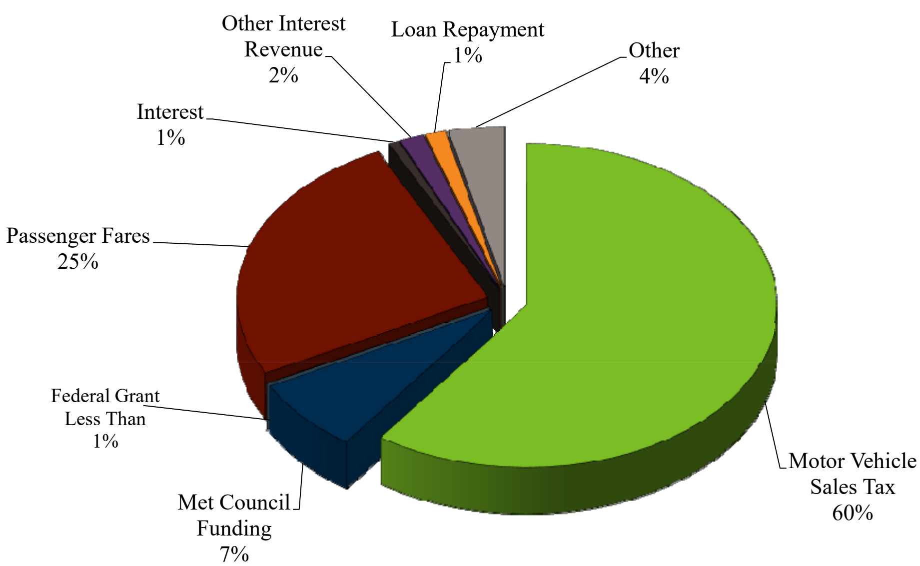
OPERATING REVENUES

The following pie charts show the allocation of revenue by source for all funds in 2018 and 2017. The most significant change between 2017 and 2018 was the result of the significant increase in regionally allocated MVST funding in 2018. As a result, the allocation of revenue by source decreased slightly for most other revenue sources.

Operating Revenues by Source for 2018 - All Funds



Operating Revenues by Source for 2017 - All Funds

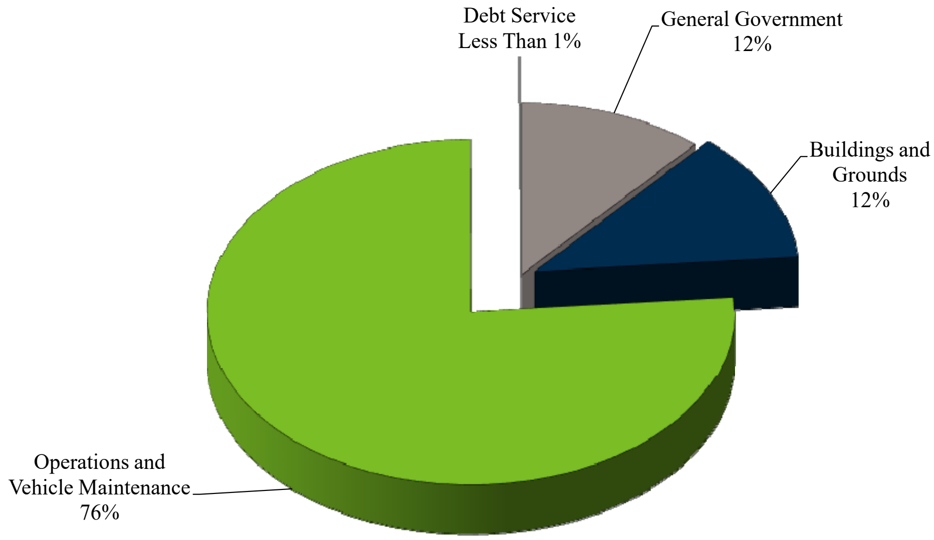


In the General Fund, the regional target for passenger farebox recovery revenue percentage in relation to operating expenditures is 28%. During 2018, SWT's passenger fare revenue as a percentage of operating expenditures was 26.10%, while it was 27.55% in 2017.

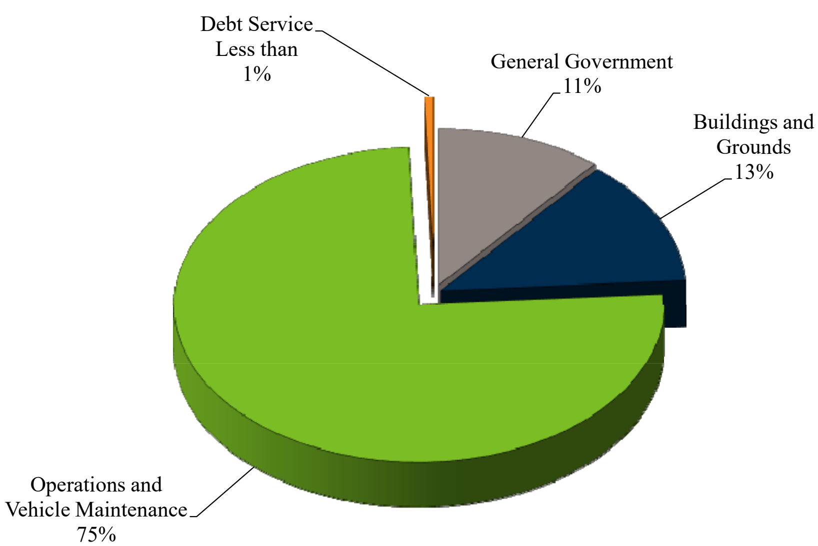
OPERATING EXPENDITURES

The following pie charts show the allocation of expenditures by program for the General Fund in 2018 and 2017. The allocation is fairly consistent with 2017.

Operating Expenditures by Department for 2018 - General Fund



Operating Expenditures by Department for 2017 - General Fund



SouthWest Transit
Emerging Issues

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. 84 – Fiduciary Activities** – GASB has issued GASB Statement No. 84 relating to accounting and financial reporting for fiduciary activities. This new statement establishes clarity to determine when a government has fiduciary responsibility for a certain activity.
- **Accounting Standard Update – GASB Statement No. 87 – Leases** – GASB has issued GASB Statement No. 87 relating to accounting and financial reporting for leases. This new statement establishes a single model for lease accounting based on the principle that leases are financing of the right to use an underlying asset.

The following are extensive summaries 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.

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 84 – *FIDUCIARY ACTIVITIES*

The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported.

This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. An exception to that requirement is provided for a business-type activity that normally expects to hold custodial assets for three months or less.

GASB Statement No. 84 describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria.

This Statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 84 – *FIDUCIARY ACTIVITIES* (CONTINUED)

GASB Statement No. 84 is effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged.

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

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 87 – *LEASES*

The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

A lease is defined as a contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified in the contract for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Any contract that meets this definition should be accounted for under the leases guidance, unless specifically excluded in this Statement.

A short-term lease is defined as a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Lessees and lessors should recognize short-term lease payments as outflows of resources or inflows of resources, respectively, based on the payment provisions of the lease contract.

A lessee should recognize a lease liability and a lease asset at the commencement of the lease term, unless the lease is a short-term lease or it transfers ownership of the underlying asset. The lease liability should be measured at the present value of payments expected to be made during the lease term (less any lease incentives). The lease asset should be measured at the amount of the initial measurement of the lease liability, plus any payments made to the lessor at or before the commencement of the lease term and certain direct costs. A lessee should reduce the lease liability as payments are made and recognize an outflow of resources (for example, expense) for interest on the liability. The lessee should amortize the lease asset in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset. The notes to financial statements should include a description of leasing arrangements, the amount of lease assets recognized, and a schedule of future lease payments to be made.

ACCOUNTING STANDARD UPDATE – GASB STATEMENT NO. 87 – *LEASES* (CONTINUED)

A lessor should recognize a lease receivable and a deferred inflow of resources at the commencement of the lease term, with certain exceptions for leases of assets held as investments, certain regulated leases, short-term leases, and leases that transfer ownership of the underlying asset. A lessor should not derecognize the asset underlying the lease. The lease receivable should be measured at the present value of lease payments expected to be received during the lease term. The deferred inflow of resources should be measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relate to future periods. A lessor should recognize interest revenue on the lease receivable and an inflow of resources (for example, revenue) from the deferred inflows of resources in a systematic and rational manner over the term of the lease. The notes to financial statements should include a description of leasing arrangements and the total amount of inflows of resources recognized from leases.

GASB Statement No. 87 is effective for reporting periods beginning after December 15, 2019. Earlier application is encouraged.

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