

Audit Committee
Honorable Mayor, George Fuller and Members of City Council
Mr. Paul G. Grimes, City Manager
Mr. Mark Holloway, Chief Financial Officer
City of McKinney
McKinney, Texas

As part of our audits of the financial statements and compliance of City of McKinney (City) as of and for the year ended September 30, 2019, we wish to communicate the following to you.

AUDIT SCOPE AND RESULTS

Auditor’s Responsibility Under Auditing Standards Generally Accepted in the United States of America and the Standards Applicable to Financial Audits Contained in Government Auditing Standards Issued by the Comptroller General of the United States and U.S. Office of Management and Budget (OMB) Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance) and the State of Texas Uniform Grant Management Standards

An audit performed in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and U.S. Office of Management and Budget (OMB) Uniform Guidance and the State of Texas *Uniform Grant Management Standards* is designed to obtain reasonable, rather than absolute, assurance about the financial statements and about whether noncompliance with the types of compliance requirements described in the OMB Compliance Supplement that could have a direct and material effect on a major federal program occurred. In performing auditing procedures, we establish scopes of audit tests in relation to the financial statements taken as a whole. Our engagement does not include a detailed audit of every transaction. Our engagement letter more specifically describes our responsibilities.

These standards require communication of significant matters related to the financial statement and compliance audits that are relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. Such matters are communicated in the remainder of this letter or have previously been communicated during other phases of the audit. The standards do not require the auditor to design procedures for the purpose of identifying other matters to be communicated with those charged with governance.

Audits of the financial statements and compliance do not relieve management or those charged with governance of their responsibilities. Our engagement letter more specifically describes your responsibilities.

Qualitative Aspects of Significant Accounting Policies and Practices

Significant Accounting Policies

The City's significant accounting policies are described in *Note 1* of the audited financial statements.

Alternative Accounting Treatments

No matters are reportable.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of financial statement preparation by management, based on its judgments. The following areas involve significant areas of such estimates for which we are prepared to discuss management's estimation process and our procedures for testing the reasonableness of those estimates:

- Useful lives of capital assets
- Allowance for doubtful accounts
- Insurance and risk management liability
- Actuarial assumptions used to estimate the net pension liability
- Actuarial assumptions used to estimate the total other postemployment benefits liabilities

Financial Statement Disclosures

The following areas involve particularly sensitive financial statement disclosures for which we are prepared to discuss the issues involved and related judgments made in formulating those disclosures:

- Defined benefit pension plans
- Other postemployment benefit plans
- Loss contingencies

Audit Adjustments

No matters are reportable.

Auditor’s Judgments About the Quality of the City’s Accounting Principles

No matters are reportable.

Other Material Communication

Listed below is a material communication between management and us related to the audit:

- Management representation letter (*attached*)

OTHER MATTERS

We observed the following matters related to ongoing standard setting by the GASB. We can discuss these matters further at your convenience and may provide assistance with implementation including initial and ongoing considerations.

GASB Statement No. 84, *Fiduciary Activities* (GASB 84)

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.

GASB 84 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 84 is effective for the City’s fiscal year ending September 30, 2020.

GASB Statement No. 87, Leases (GASB 87)

GASB 87 provides a new framework for accounting for leases under the principle that leases are financings. No longer will leases be classified between capital and operating. Lessees will recognize an intangible asset and a corresponding liability. The liability will be based on the payments expected to be paid over the lease term, which includes an evaluation of the likelihood of exercising renewal or termination options in the lease. Lessors will recognize a lease receivable and related deferred inflow of resources. Lessors will not derecognize the underlying asset. An exception to the general model is provided for short-term leases that cannot last more than 12 months. Contracts that contain lease and non-lease components will need to be separated so each component is accounted for accordingly. GASB 87 is effective for the City's fiscal year ending September 30, 2021. Governments will be allowed to transition using the facts and circumstances in place at the time of adoption, rather than retroactive to the time each lease was begun.

This communication is intended solely for the information and use of the Audit Committee, City Council and management, and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

January 29, 2020



January 29, 2020

BKD, LLP
Certified Public Accountants
14241 Dallas Parkway, Suite 1100
Dallas, Texas 75254

We are providing this letter in connection with your audit of our financial statements as of and for the year ended September 30, 2019 and your audit of our compliance with requirements applicable to each of our major federal and state awards programs as of and for the year ended September 30, 2019. We confirm that we are responsible for the fair presentation of the financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining effective internal control over financial reporting, operations and compliance, and preventing and detecting fraud.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following:

1. We have fulfilled our responsibilities, as set out in the terms of our engagement letter dated July 12, 2019, for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America.
2. We acknowledge our responsibility for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.
3. We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.

Finance Department

P.O. Box 517 • McKinney, Texas 75070 • Metro 972-562-6080

4. We have reviewed and approved a draft of the financial statements and related notes referred to above, which you prepared in connection with your audit of our financial statements. We acknowledge that we are responsible for the fair presentation of the financial statements and related notes.
5. We have provided you with:
 - (a) Access to all information of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation and other matters.
 - (b) Additional information that you have requested from us for the purpose of the audit.
 - (c) Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
 - (d) All minutes of meetings of the governing body held through the date of this letter.
 - (e) All significant contracts and grants.
6. All transactions have been recorded in the accounting records and are reflected in the financial statements.
7. We have informed you of all current risks of a material amount that are not adequately prevented or detected by entity procedures with respect to:
 - (a) Misappropriation of assets.
 - (b) Misrepresented or misstated assets, liabilities or net position.
8. We understand the potential penalties for failure to disclose reportable tax transactions to the taxing authorities and have fully disclosed to BKD any and all known reportable tax transactions.
9. We have no knowledge of any known or suspected:
 - (a) Fraudulent financial reporting or misappropriation of assets involving management or employees who have significant roles in internal control.
 - (b) Fraudulent financial reporting or misappropriation of assets involving others that could have a material effect on the financial statements.

10. We have no knowledge of any allegations of fraud or suspected fraud affecting the City received in communications from employees, customers, regulators, suppliers or others.
11. We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America. We understand that the term related party refers to an affiliate; management, and members of their immediate families, component units; and any other party with which the entity may deal if it can significantly influence, or be influenced by, the management or operating policies of the other. The term affiliate refers to a party that directly or indirectly controls, or is controlled by, or is under common control with us.
12. Except as reflected in the financial statements, there are no:
 - (a) Plans or intentions that may materially affect carrying values or classifications of assets and liabilities.
 - (b) Material transactions omitted or improperly recorded in the financial statements.
 - (c) Material gain/loss contingencies requiring accrual or disclosure, including those arising from environmental remediation obligations.
 - (d) Events occurring subsequent to the balance sheet date through the date of this letter requiring adjustment or disclosure in the financial statements.
 - (e) Agreements to purchase assets previously sold.
 - (f) Restrictions on cash balances or compensating balance agreements.
 - (g) Guarantees, whether written or oral, under which the City is contingently liable.
13. We have disclosed to you all known instances of noncompliance or suspected noncompliance with laws and regulations whose effects should be considered when preparing financial statements.
14. We have no reason to believe the City owes any penalties or payments under the Employer Shared Responsibility Provisions of the Patient Protection and Affordable Care Act nor have we received any correspondence from the IRS or other agencies indicating such payments may be due.

15. We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America.
16. Adequate provisions and allowances have been accrued for any material losses from:
 - (a) Uncollectible receivables.
 - (b) Reducing obsolete or excess inventories to estimated net realizable value.
 - (c) Sales commitments, including those unable to be fulfilled.
 - (d) Purchase commitments in excess of normal requirements or above prevailing market prices.
17. Except as disclosed in the financial statements, we have:
 - (a) Satisfactory title to all recorded assets, and they are not subject to any liens, pledges or other encumbrances.
 - (b) Complied with all aspects of contractual and grant agreements, for which noncompliance would materially affect the financial statements.
18. We have no asset retirement obligations required to be reported by GASB Statement No. 83, *Certain Asset Retirement Obligations*.
19. We have not been designated as a potentially responsible party (PRP or equivalent status) by the Environmental Protection Agency (EPA) or other cognizant regulatory agency with authority to enforce environmental laws and regulations.
20. We have notified you of any instances of noncompliance with applicable disclosure requirements of the SEC Rule 15c2-12 and applicable state laws.
21. With regard to deposit and investment activities:
 - (a) All deposit, repurchase and reverse repurchase agreements and investment transactions have been made in accordance with legal and contractual requirements.
 - (b) Disclosures of deposit and investment balances and risks in the financial statements are consistent with our understanding of the applicable laws regarding enforceability of any pledges of collateral.

- (c) We understand that your audit does not represent an opinion regarding the enforceability of any collateral pledges.
22. With respect to any nonattest services you have provided us during the year, including assistance with preparation of our draft comprehensive annual financial report:
- (a) We have designated a qualified management-level individual to be responsible and accountable for overseeing the nonattest services.
 - (b) We have established and monitored the performance of the nonattest services to ensure that they meet our objectives.
 - (c) We have made any and all decisions involving management functions with respect to the nonattest services and accept full responsibility for such decisions.
 - (d) We have evaluated the adequacy of the services performed and any findings that resulted.
23. We acknowledge that we are responsible for compliance with applicable laws, regulations and provisions of contracts and grant agreements.
24. We have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that have a direct and material effect on the determination of amounts in our financial statements or other financial data significant to the audit objectives.
25. We have identified and disclosed to you any violations or possible violations of laws, regulations and provisions of contracts and grant agreements whose effects should be considered for recognition and/or disclosure in the financial statements or for your reporting on noncompliance.
26. We have taken or will take timely and appropriate steps to remedy any fraud, abuse, illegal acts or violations of provisions of contracts or grant agreements that you or other auditors report.
27. We have a process to track the status of audit findings and recommendations.
28. We have identified to you any previous financial audits, attestation engagements, performance audits or other studies related to the objectives of your audit and the corrective actions taken to address any significant findings and recommendations made in such audits, attestation engagements or other studies.

29. We have provided our views on any findings, conclusions and recommendations, as well as our planned corrective actions with respect thereto, to you for inclusion in the findings and recommendations referred to in your report on internal control over financial reporting and on compliance and other matters based on your audit of the financial statements performed in accordance with *Government Auditing Standards*.
30. With regard to federal awards programs:
- (a) We have identified in the schedule of expenditures of federal awards all assistance provided (either directly or passed through other entities) by federal agencies in the form of grants, contracts, loans, loan guarantees, property, cooperative agreements, interest subsidies, commodities, insurance, direct appropriations or in any other form.
 - (b) We have identified the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Compliance Supplement* regarding activities allowed or unallowed; allowable costs/cost principles; cash management; eligibility; equipment and real property management; matching, level of effort, earmarking; period of performance of federal funds; procurement and suspension and debarment; program income; reporting; subrecipient monitoring; and special tests and provisions that are applicable to each of our federal awards programs. We have identified to you our interpretation of any applicable compliance requirements subject to varying interpretations.
 - (c) We are responsible for complying, and have complied, with the requirements of Uniform Guidance.
 - (d) We are responsible to understand and comply with the requirements of federal statutes, regulations and the terms and conditions of federal awards related to each of our federal awards programs and have disclosed to you any and all instances of noncompliance with those requirements occurring during the period of your audit or subsequent thereto to the date of this letter of which we are aware. Except for any instances of noncompliance, we have disclosed to you, we believe the City has complied with all applicable compliance requirements.
 - (e) We are responsible for establishing and maintaining effective internal control over compliance to provide reasonable assurance we have administered each of our federal awards programs in compliance with federal statutes, regulations and the terms and conditions of the federal awards.

- (f) We have made available to you all federal awards (including amendments, if any) and any other correspondence or documentation relevant to each of our federal awards programs and to our compliance with applicable requirements of those programs.
- (g) The information presented in federal awards program financial reports and claims for advances and reimbursements is supported by the books and records from which our financial statements have been prepared.
- (h) The costs charged to federal awards are in accordance with applicable cost principles.
- (i) The reports provided to you related to federal awards programs are true copies of reports submitted or electronically transmitted to the federal awarding agency, the applicable payment system or pass-through entity in the case of a subrecipient.
- (j) Amounts claimed or used for matching were determined in accordance with Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) regarding cost principles.
- (k) We have monitored any subrecipients to determine that they have expended federal awards in accordance with federal statutes, regulations and the terms and conditions of the subaward and have met the audit and other requirements of the Uniform Guidance.
- (l) We have taken appropriate corrective action on a timely basis after receipt of any subrecipient's auditor's report that identified findings and questioned costs pertaining to federal awards programs passed through to the subrecipient by us.
- (m) We have considered the results of any subrecipient's audits received and made any necessary adjustments to our books and records.
- (n) We have disclosed to you any communications from federal awarding agencies and pass-through entities concerning possible noncompliance with the applicable compliance requirements for each of our federal awards programs, including any communications received from the end of the period of your audit through the date of this letter.

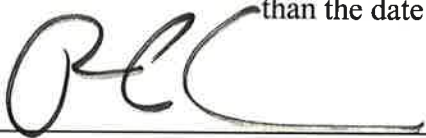
- (o) We have identified to you any previous compliance audits, attestation engagements and internal or external monitoring related to the objectives of your compliance audit, including findings received and corrective actions taken to address any significant findings and recommendations made in such audits, attestation engagements or other monitoring.
- (p) We are responsible for taking corrective action on any audit findings.
- (q) The reporting package does not contain any protected personally identifiable information.

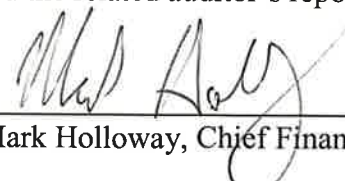
31. With regard to state awards programs:

- a) We have identified in the schedule of expenditures of state awards all assistance provided (either directly or passed through other entities) by state agencies in the form of grants, contracts, loans, loan guarantees, property, cooperative agreements, interest subsidies, commodities, insurance, direct appropriations or in any other form.
- b) We have identified the types of compliance requirements described in the Texas Uniform Grants Management Standards issued by the Governor's Office of Budget and Management of the State of Texas regarding activities allowed or unallowed; allowable costs/cost principles; cash management; Davis-Bacon Act; eligibility; equipment and real property management; matching, level of effort, earmarking; period of performance of state funds; procurement and suspension and debarment; program income; real property acquisition and relocation assistance; reporting; subrecipient monitoring; and special tests and provisions that are applicable to each of our state awards programs. We have identified to you our interpretation of any applicable compliance requirements subject to varying interpretations.
- c) We are responsible to understand and comply with the requirements of laws, regulations, contracts and grants applicable to each of our state awards programs and have disclosed to you any and all instances of noncompliance with those requirements occurring during the period of your audit or subsequent thereto to the date of this letter of which we are aware. Except for any instances of noncompliance, we have disclosed to you, we believe the City has complied with all applicable compliance requirements.
- d) We are responsible for establishing and maintaining effective internal control over compliance to provide reasonable assurance we have administered each of our state awards programs in compliance with requirements of laws, regulations, contracts and grants applicable to those programs.

- e) We have made available to you all contracts and grant agreements, including any amendments, and any other correspondence or documentation relevant to each of our state awards programs and to our compliance with applicable requirements of those programs.
 - f) The information presented in state awards program financial reports and claims for advances and reimbursements is supported by the books and records from which our financial statements have been prepared.
 - g) The reports provided to you related to state awards programs are true copies of reports submitted or electronically transmitted to the state awarding agency, the applicable payment system or pass-through entity in the case of a subrecipient.
 - h) Amounts claimed or used for matching were determined in accordance with the applicable Texas Uniform Grant Management Standards regarding cost principles.
 - i) We have disclosed to you any communications from grantors and pass-through entities concerning possible noncompliance with the applicable compliance requirements for each of our state awards programs, including any communications received from the end of the period of your audit through the date of this letter.
 - j) We have identified to you any previous compliance audits, attestation engagements and internal or external monitoring related to the objectives of your compliance audit, including findings received and corrective actions taken to address any significant findings and recommendations made in such audits, attestation engagements or other monitoring.
32. The financial statements disclose all significant estimates and material concentrations known to us. Significant estimates are estimates at the balance sheet date which could change materially within the next year. Concentrations refer to volumes of business, revenues, available sources of supply, or markets for which events could occur which would significantly disrupt normal finances within the next year. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

33. The fair values of financial and nonfinancial assets and liabilities, if any, recognized in the financial statements or disclosed in the notes thereto are reasonable estimates based on the methods and assumptions used. The methods and significant assumptions used result in measurements of fair value appropriate for financial statement recognition and disclosure purposes and have been applied consistently from period to period, taking into account any changes in circumstances. The significant assumptions appropriately reflect market participant assumptions.
34. The supplementary information required by the Governmental Accounting Standards Board, consisting of management's discussion and analysis and pension and other postemployment benefit information has been prepared and is measured and presented in conformity with the applicable GASB pronouncements, and we acknowledge our responsibility for the information. The information contained therein is based on all facts, decisions and conditions currently known to us and is measured using the same methods and assumptions as were used in the preparation of the financial statements. We believe the significant assumptions underlying the measurement and/or presentation of the information are reasonable and appropriate. There has been no change from the preceding period in the methods of measurement and presentation.
35. With regard to supplementary information:
- (a) We acknowledge our responsibility for the presentation of the supplementary information in accordance with the applicable criteria.
 - (b) We believe the supplementary information is fairly presented, both in form and content, in accordance with the applicable criteria.
 - (c) The methods of measurement and presentation of the supplementary information are unchanged from those used in the prior period.
 - (d) We believe the significant assumptions or interpretations underlying the measurement and/or presentation of the supplementary information are reasonable and appropriate.
 - (e) If the supplementary information is not presented with the audited financial statements, we acknowledge we will make the audited financial statements readily available to intended users of the supplementary information no later than the date such information and the related auditor's report are issued.


Paul G. Grimes, City Manager


Mark Holloway, Chief Financial Officer