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Audit Committee, City Council and Management
City and County of Denver
Denver, Colorado

In planning and performing our audit of the financial statements of **CITY AND COUNTY OF DENVER** (the City) as of and for the year ended December 31, 2017, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City'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 significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

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 of the City's financial statements on a timely basis. A deficiency in design exists when a control necessary to meet a control objective is missing or an existing control is not properly designed so that, even if the control operates as designed, a control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A significant deficiency is a deficiency, or 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.

A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented or detected and corrected on a timely basis.

We observed the following matters that we consider to be deficiencies, significant deficiencies or material weaknesses.

MATERIAL WEAKNESSES

2017-001 The Airport – Accounts Receivable

Criteria or Specific Requirement: Management is responsible for establishing and maintaining effective internal controls over financial reporting. Effective internal controls are an important component of a system that helps ensure transactions are recorded timely and in the proper reporting period, thereby providing accurate financial data. Specifically, the Airport should have controls in place to ensure the Airport's revenue is properly recorded, and payments received from customers are either properly applied to outstanding receivables or recorded as unearned.

Condition: During the 2017 audit of accounts receivable, there were instances of misapplication of payments received to accounts receivable and liabilities resulting in a gross up of the statement of net position. When viewed in the aggregate, the issues detailed below are indicative of a larger internal control issue. The following instances were observed during the audit:

1. City fuel tax payments related to 2016 for approximately $2.5 million were recorded as revenue in 2017. Revenue in the current year is overstated by this amount.
2. Fuel tax payments for approximately $1.9 million received from the State of Colorado were incorrectly recorded as a liability at year-end, rather than as 2017 revenue. After the Airport accounting attempted to correct the issue, the adjustment was posted to accounts receivable rather than reduce the unapplied payments liability and record revenue. Receivables are overstated by $1.9 million.
3. An advanced rental payment (liability) of $4.2 million was received from an airline relating to 2018 rents, but the payment was recorded as a reduction to unrelated receivables rather than as an advanced rent payment for subsequent year rents. Receivables are understated by $4.2 million.
4. At year-end, the Airport had recorded a $1.7 million receivable for catering revenue. However, prior to year-end, payment was received on this balance and was recorded as a liability instead of being properly credited against the receivable. Therefore, the Airport's liability and receivable are overstated by $1.7 million.
5. A credit was posted as a reduction to the landing fees receivable in anticipation of the impact of the annual year-end rates and charges true-up calculation, leaving an estimated remaining receivable from the airlines at year-end. When the rates and charges true-up calculation was recorded, the entire amount was recorded as a liability rather than reducing the remaining receivable for approximately $6 million. Therefore, both receivables and liabilities are overstated at year-end.

Effect: The items outlined above resulted in adjustments proposed which were not recorded by the Airport as these entries did not have an impact on the statement of revenues, expenses and changes in net position.

Cause:
(A) For revenues recorded in the incorrect period, Airport accounting examines subsequent cash receipts when reconciling accounts receivable at year-end in preparation for the annual financial audit. The conversion to a new general ledger system (and the intricacies of the revenue module within the new system) created many difficulties that resulted in accounts receivable reconciliations not being performed until after year-end. Consequently, there were multiple instances of improper accrual of revenue, or receivables not being relieved by payments received.

(B) The general ledger includes unapplied cash receipts for which there are related receivables. Discussions with Airport accounting disclosed that the issue is caused by payees not providing enough detail to allow appropriate application. The result is the Airport recording the cash received as an unapplied payment until matched to the related receivable. Subsequent to year-end, many payments had not been applied to the related receivable, resulting in the gross up of assets and liabilities on the statement of net position.

Recommendation: We recommend that reconciliation of accounts receivable and unapplied payments be performed on a consistent, monthly basis to properly match payments with customer receivables or customer pre-payments.

Views of Responsible Officials and Planned Corrective Actions: The Airport agrees with the finding. See separate report for planned corrective actions.

2017-002 The Airport – Accounting for Grant Revenue

Criteria or Specific Requirement: The Airport System, as an enterprise fund, uses the full accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized as incurred. Governmental Accounting Standards Board (GASB) Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, prescribes revenue should be recognized when eligibility requirements of reimbursement-type grants have been met. That is, the recipient should record revenue when meeting the provider's requirements by incurring costs in accordance with the provider's program.

Condition: The Airport under-reported Federal grant revenue, as revenue was not being recognized upon recognition of incurred costs associated with the Federal programs in 2016 and 2017.

Effect: An adjustment of $12.2 million to increase grant revenue in 2017 was proposed and recorded by the Airport System. Additionally, $2.1 million of grant revenue earned in 2016 was recorded in 2017; therefore, revenue was overstated in 2017 by $2.1 million.

Cause: Airport System management interpreted GASB Statement No. 33 as revenue should be recognized as eligible and recorded upon approval and reimbursement by the Federal granting agency. This interpretation caused timing delays between costs recorded in the general ledger and the associated earned revenue. In the second instance as outlined above, the delay in timing crossed fiscal years.

Recommendation: We recommend the Airport System record revenue when eligible and earned as costs are being incurred and recorded in the Airport System's records.

Views of Responsible Officials and Planned Corrective Actions: The Airport adjusted grant revenue to reflect expenses incurred for the year ended December 31, 2017; however the Airport still takes the position to report only the requested for reimbursement rather than total actual expenditures incurred, based on determination of allowability by the Federal Agency. This determination was based on GASB Statement No. 33 definition of eligibility requirements for reimbursements as "....incurred allowable costs under the applicable program." As it relates to the Federal programs in question, allowable costs is typically determined by the provider when the reimbursement request have been approved. The Airport is seeking guidance from the Federal agencies on the determination on when an expenditure is considered allowable, since industry-wide there is a disparity. The Airport has found that there are conflicting audit opinions across the industry and has taken the conservative approach in recording grant revenue.

Auditor's Response: We disagree with the auditees' planned corrective actions. GASB 33 paragraph 20.C indicates that eligibility requirements of a grant may include reimbursement restrictions that require the auditee to have incurred allowable costs under the applicable program; however, the Airport has indicated above that allowability is determined by the grantor through approval of reimbursement requests. 2 Part 200.303 Internal Controls, indicates that the non-Federal entity must establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. As such, the Airport should have internal controls in place to determine allowability and should not be reliant on the grantor for this determination.

2017-004 Schedule of Expenditures of Federal Awards Preparation

Criteria or Specific Requirement: In accordance with 2 Part 200.510, auditees receiving Federal funds must prepare an annual Schedule of Expenditure of Federal Awards (SEFA) detailing the value and type of Federal assistance received each year. The Federal Office of Management and Budget issues instructions on how to prepare this schedule. Key information to be reported includes the catalog of Federal domestic assistance (CFDA) number provided in the Federal awards/subaward agreements and associated expenditures incurred in the fiscal year. At the City and County of Denver, the SEFA is prepared by the Controller's Office based on information from the accounting system and additional information provided by the various departments receiving Federal funds.

Condition: (A) Federal expenditure amounts reported by Denver International Airport related to the Airport Improvement Program failed to include expenditures that had not been requested for reimbursement.

(B) Federal expenditure amounts reported by the Department of Public Health & Environment (the Department) included estimated expenditures based on unbilled subreceipient contracts.

Context: (A) Total expenditures of $11.9 million originally reported for the Airport Improvement Program were increased by $3.0 million to bring the final expenditures total for the program to $14.9 million for the year ended December 31, 2017.

(B) Total expenditures for the HIV Emergency Relief Project Grants were reduced by $271,000 to bring the final expenditure total for the program to $7.5 million for the year ended December 31, 2017.

Effect: The Federal government and pass-through entities rely on the SEFA information to be reported accurately. In addition, accurate SEFA information is relied upon by the auditors in order to perform the major program determination utilized to select the Federal programs subjected to single audit procedures.

Cause: Grant management at the City is decentralized and thus departments are responsible for providing the required information to the City's Controller's Office to facilitate the preparation of the SEFA.

(A) The amounts provided by Airport personnel included only amounts that had been requested for reimbursement rather than total actual expenditures incurred.

(B) The Department experienced significant delays in receiving requests for reimbursement from subrecipients and therefore estimated expenditures for program management purposes and general ledger reporting without considering the implications for SEFA reporting.

Recommendation: (A) We recommend that all Federal expenditures be identified and reconciled to the general ledger and reported on the SEFA for the Airport Improvement Program.

(B) We recommend that the Department implement procedures to better manage the subrecipient reimbursement process to ensure that requests for reimbursement are received in a timely manner eliminating the need for estimates.

Views of Responsible Officials and Planned Corrective Actions: (A) The Airport understands the City reports on an accrual basis for the Schedule of Expenditures of Federal Awards (SEFA) and has agreed to the appropriate adjustments for the year ended December 31, 2017 but believes there is inconsistency in industry practice and is seeking guidance from the Federal Aviation Administration (FAA) to support continuing to report expenditures as described in the cause above.

(B) The Department of Public Health & Environment agrees with the finding. See separate report for planned corrective actions.

Auditor's Response: We believe the Airport's suggested approach is not an option under the AICPA Government Auditing Standards and Single Audits — Clarified Chapter 7.07 Basis of Accounting and 2 Part 200.502 Basis for determining Federal awards expended, which indicates the determination of when a Federal award is expended must be based on when the activity related to the Federal award occurs. Generally, the activity pertains to events that require the non-Federal entity to comply with Federal statutes, regulations, and the terms and conditions of Federal awards, such as: expenditure/expense transactions associated with awards including grants. We believe the options available are the accrual basis as expenditures are incurred or cash basis when expenditures are paid. The FAA request for reimbursement and approval process is irrelevant to the reporting of expenditures on the SEFA.

SIGNIFICANT DEFICIENCY

2017-003 Capital Assets

Criteria or Specific Requirement: Accounting principles generally accepted in the United States of America (US GAAP) that addresses the proper recognition and accounting of capital assets includes:

- Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments* (GASB 34)
- Governmental Accounting Standards Board (GASB) Statement No. 37, *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments: Omnibus — an amendment of GASB Statements No. 21 and No. 34* (GASB 37)
- Governmental Accounting Standards Board (GASB) Statement No.51, *Accounting and Financial Reporting for Intangible Assets* (GASB 51)
- Various implementation guidance issued by GASB

Condition: Several issues were noted relating to capital assets including:

- During fiscal year 2017, the City implemented a new ERP system called "Workday." Due to this implementation the City revised its method of compiling documentation, and the City had difficulty in providing detailed populations, especially for construction in process (CIP). This resulted in us expanding our additions and disposals testing to specifically include identified assets that were added or disposed of during the fiscal year. We discovered errors in the recognition of additions and disposals for certain assets. While these errors were not material, we noted cutoff issues where assets were placed in service in an earlier period but not included in capital assets until the current period or disposed of in an earlier period and not removed from the system until the current year. We also noted assets that were erroneously deleted from the system, prior to the conversion to the Workday system, while the assets were still in service.
- Approximately \$6.6M of project costs that should have been expensed in the prior year remained in the CIP balances at year-end and as a result overstated the project balance as of December 31, 2017.
- Clerical errors were noted where costs transferred out of CIP were not properly registered within Workday and where agencies did not timely report their CIP activities in Workday prior to closing the capital asset "book." This necessitated manual entries to be performed to record the activity. While these issues did not result in material errors or audit adjustments, they do show a need to strengthen controls.
- Approximately \$1.8M of project costs were improperly expensed out of CIP.

Effect: The conditions noted above resulted in several proposed adjustments to capital asset balances, which the City chose not to record. These issues also created inefficiencies and difficulties in the audit process for both BKD and management.

Cause: As mentioned, the City implemented the new Workday ERP system, and the conversion of data formerly contained in the PeopleSoft system to the Workday system created some difficulties and caused some of the issues noted above. In other cases, established internal controls were not effective in preventing or detecting and correcting clerical errors in the recording and recognition of capital assets in a timely manner.

Recommendation: We recommend that internal controls continue to be strengthened over the new Workday system, especially in the form of reconciling the capital asset data as necessary. Training should also continue for Controller Office staff with responsibility over capital assets to ensure successful cross-training of functions and understanding of the Workday system. Lastly, we recommend the City continue to develop standard audit workpapers from the Workday system that will facilitate the support of capital asset transactions and balances.

Views of Responsible Officials and Planned Corrective Actions: The City agrees with the finding. See separate report for planned corrective actions.

DEFICIENCIES

2017 D-1 Traffic Signal Additions and Deletions

Finding: When recording capital asset additions for traffic signals built by outside contractors, the City's practice is to capitalize the average amount for each signal outlined in the contractor's bid document, rather than the actual cost of the individual traffic signal. During testing of Contractor Build Traffic Signal additions, we noted that the fiscal year 2015 estimate was used when determining the fiscal year 2017 additions amount. Furthermore, the City uses a "first in, first out" approach when disposing of traffic signals. Instead of writing off the actual item that was disposed or replaced, the City removes the oldest remaining traffic signal from its capital asset inventory. The net result of this procedure is not material and did not result in adjustment, but could potentially lead to material errors.

Recommendation: We recommend that the estimate for Contractor Built Traffic Signals be updated annually and determined using a broad range of projects to help ensure a more accurate estimate. In addition, we recommend that the City remove the actual traffic signal being removed or replaced rather than the oldest in-service signal.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Public Works is actively addressing the methodology used to determine the value of assets built in-house. A computerized asset management system, Cartegraph, was purchased. Cartegraph is a software program specifically designed for Public Works departments to track the cost associated with individual assets, like traffic signals. This will be used for all new projects, but a cost benefit analysis will be conducted to determine if historical cost data can be implemented in a timely manner. An Assets Policy and Procedure has been written and Public Works will follow BKD's recommendation of disposing the asset being replaced rather than removing items from the capital asset list on a first-in, first-out basis.

Person(s) responsible for implementing: Kristi Torres, Department of Public Works Financial Manager.
Implementation date: Already implemented.

2017 D-2 Long-term Receivables

Finding: During our testing of long-term accounts receivable, we noted the following issues:

- Due to a clerical error, accounts receivable and the allowance for the County Court was overstated, as the incorrect balance was being used by the City to calculate the collectible amount of accounts receivable at year-end. This resulted in proposed adjustments of $2.9 million and $2.6 million, to accounts receivable and allowance, respectively. The City chose not to record these proposed adjustments.
- The City revised the methodology used to compute the Public Works accounts receivable balance at year-end. Historically, the City used a 2-year look-back to determine the gross receivables balance and the same look-back period to compute the collectible amount, the inverse of which comprises the allowance on the long-term receivables. In the current year, the City revised this methodology from a 2-year period to a 3-year period as the basis for reporting the gross receivable. However, when changing this methodology, the City maintained the 2-year look-back period to compute the collectible portion of receivables. The resulting difference was not material to the financial statements, but for consistency a 3-year period should be used when computing the collectible portion of receivables and therefore the allowance on those receivables.

Recommendation: If the City will continue to use a 3-year look-back period when determining the year-end balance of long-term receivables for Public Works, this same period should be used to calculate the collectible portion and therefore the allowance on those receivables.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. The error for County Court was due to a formula error in the reporting package used to report the balance to the Controller's Office. As soon as the error was identified, it was corrected so the proper balance will be reported going forward. Going forward, Public Works will ensure that a 3-year look back period is used when determining the year-end balance of long-term receivables. The same 3-year look back period will be used to calculate the collectible portion and therefore the allowance on the receivables. When presented with a situation where there is less than a 4% return, a longer look period will be used.

Person(s) responsible for implementing: Stacie Beckwith, Denver County Courts Financial Manager, and Kristi Torres, Department of Public Works Financial Manager.
Implementation date: Already implemented.

2017 D-3 Grants Receivable

Finding: The City was unable to provide adequate substantive support for certain grants receivable balances in the human services fund. This resulted in a proposed adjustment to this fund of $290,000 to reduce the balance. The City chose not to record this adjustment.

In addition, as the City implemented the new Workday system during fiscal year 2017, certain reports and reconciliations were not available or not performed at year-end. For example, a grant receivable rollforward was not prepared this year, as had historically been done. The rollforward process is an integral tool in supporting management's assertion over completeness of the grants receivable balances and is also important to the testing of the Scheduled of Expenditures of Federal Awards. Furthermore, the City was unable to provide a listing of cash receipts received under each individual grant, which made the audit process cumbersome and significantly increased the difficulty for the City to substantiate these balances. Lastly, we discovered that information that should have been uploaded to the Workday system during the system conversion process was not done consistently, which further increased the City's difficulty in providing support for year-end balances.

Recommendation: We believe that many of the issues identified above will be corrected as the City's use of Workday expands. However, we recommend that the City develop a rollforward process for grants receivable in order to compile this important document for year-end. Ideally, the grant rollforward process should be performed on a quarterly basis to ease the burden of preparing the rollforward at year-end. The development of a cash receipts report by individual grants would greatly assist in the compilation of a rollforward. Furthermore, all documentation should be maintained and available at year-end to support all recorded balances.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. The State was, and currently still is, having problems with their new reimbursement system that has resulted in delayed reimbursements for allowable expenditures at DDHS. Approximately $60,000 was not received promptly due to this issue. As of June 2018, these amounts have been reimbursed to DDHS. The remaining $224,000 resulted from the expenditure contract with the subrecipient being written to include unallowable costs. A request for reimbursement was initiated, and denied by the grantor, the U.S. Department of Housing and Urban Development (HUD), and the costs will be moved to DDHS General funds. These expenditure types will no longer be submitted for reimbursement.

Additionally, Workday automatically calculates the grants receivable balance based on expenditures recorded to the grant program which the City believes will ultimately help strengthen and improve the reporting of grants receivable balance. Controller's Office is currently evaluating and testing different methodologies to capture cash receipt information in order to prepare a grant receivable rollfoward as we have historically.
Person(s) responsible for implementing: Mikki Harville, Accounting Supervisor, DDHS, and Shanna Tohill, Manager of Financial Reporting.
Implementation date: August 31, 2018 and April 1, 2019.

2017 D-4 Disaster Recovery Plan

Finding: The Information Technology Disaster Recovery Policy dated September 11, 2017 requires that the City annually test the disaster recovery plan and procedures in a suitable environment to ensure that the systems, networks, databases and other IT infrastructure elements can be recovered and returned to normal operations in the event of an unplanned interruption and that designated disaster recovery team members and other participants remain familiar with the disaster recovery plan and procedures as well as their respective roles and responsibilities. During our review of the documentation provided and inquiry of the City's personnel, we determined that the City has never performed a full backup recovery test of its critical financial sub-systems including GenTax, Oasis and ECS. Although the City performs individual recoveries when a file or a folder is lost or accidentally deleted, the restorability of critical financial systems has not been fully tested.

Recommendation: In compliance with policy, we recommend the City perform an annual documented restoration test of financial applications and data.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Since the Disaster Recovery Policy was recently published on September 11, 2017, we need to allow time for the policy to be adopted and set a target date for the annual test of the disaster recovery plan and procedures, including a full backup recovery test of financial applications and data.

Person(s) responsible for implementing: James Stoner, Chief Information Security Architect.
Implementation date: December 31, 2018.

2017 D-5 Back Up Data Center Location

Finding: The City's secondary data center is located within the City limits, less than five miles from the primary data center. Given their proximity, both data centers could be affected by the same regional events resulting in an extended service outage. Although these two data centers may be impacted by the same regional events, the City has elected to accept this risk for economic and other business reasons.

Recommendation: We recommend that the City move the secondary data center further away from the primary data center. Best practices suggest the secondary data center are on a different power grid.

Views of Responsible Officials and Planned Corrective Actions: Technology Services accepts the risk for this finding. The City is a municipality and our staff is located in the Denver metropolitan area.

Person(s) responsible for implementing: Not Applicable.
Implementation date: Not Applicable.

2017 D-6 Review of Access Privileges

Finding: Per our review of access privileges for the in-scope applications, an annual review of user access (re-certification) is not performed by the business owners. Periodic re-certification helps control risks associated with segregation of duties issues arising from personnel changing functional responsibilities and unauthorized access resulting from delays in disabling accounts for terminated users.

Recommendation: Although the review may be coordinated by Technology Services, we recommend that the City's business owners perform a periodic documented review of logical access for users of applications supporting general ledger and its supporting sub-systems, databases and operating systems.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Technology Services will provide business owners with user access lists for the in-scope applications so that they may perform periodic access reviews.

Person(s) responsible for implementing: Tricia Scherer, IT Governance Manager.
Implementation date: December 31, 2018.

2017 D-7 Vendor Management

Finding: Although some portions have been completed and implemented, the Technology Services department has not completed its comprehensive policy for vendor management. Vendor management policy helps to effectively manage the lifecycle of all vendor relationships to responsibly steward resources and minimize the inherent risk associated with engaging third parties to perform services.

Recommendation: We recommend that the City finalize its comprehensive vendor management policy which will include periodic after-award reviews of third-party service provider's Service and Organization Controls (SOC) Reports.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Technology Services will finalize and publish its Vendor Management Policy before year-end, 2018. The policy will include after-award reviews of third-party service provider's SOC Reports.

Person(s) responsible for implementing: Tricia Scherer, IT Governance Manager.
Implementation date: December 31, 2018.

2017 D-8 Information Security Systems and Cyber Security Standards

Finding: An initiative was undertaken by the City's Auditor's Office in 2016 to evaluate the City's information network and information technology security. A report issued by Hein & Associates LLP – CCD titled 'Information Systems Maturity Assessment' dated March 16, 2017, identified multiple areas for improvement. Although several risk areas had been addressed to date, not all risks had been fully addressed at the time of our review.

Recommendation: We recommend that the City continue to work on recommended actions to enhance cybersecurity surrounding its financial applications, sub-systems, and supporting infrastructure. The City could benefit by performing security risk assessments that employ the enterprise risk assessment approach and include all stakeholders to ensure that all aspects of the IT organization are addressed, including hardware and software, employee awareness training, and business processes.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Technology Services will continue to remediate the findings from the referenced Information Systems Maturity Assessment. In addition, Technology Services will consider expanding its current risk assessment process for PCI systems to include hardware and other financial applications. Technology Services already deploys annual required cybersecurity awareness training city-wide.

Person(s) responsible for implementing: Tricia Scherer, IT Governance Manager.
Implementation date: December 31, 2018.

2017 D-9 The Airport Policy Documents

Finding: During our audit, we noted that the business technology digital strategy, change management policy and processes, Information Security Program Standard, Acceptable Use Policy, User and Remote Access agreement, Physical Security Standards, Un-badged Data Center Access Procedures, Continuity of Operation/Pandemic Plan documents provided to us were not approved by a responsible official. The Continuity of Operation Plan, which is also a disaster recovery plan, has not been reviewed and updated since March 2013.

Recommendation: We recommend that the Airport formally approve all policies to ensure and enforce the applicability in the organization. We further recommend that the Airport develop a practice of reviewing and updating the policies and procedures annually.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. Pending capital funding approval, DEN Business Technologies will engage a professional services vendor to implement the ServiceNow Governance Risk and Compliance (GRC) Module with Document Management functionality. This will provide the semi-automated document review processes and actionable approval workflows required to more effectively manage our policies and procedures.

Person(s) responsible for implementing: Tim Coogan, Chief Information Security Officer.
Implementation date: June 30, 2019.

2017 D-10 The Airport Testing of Backup Data

Finding: Per discussion with the Airport, there was no major backup restoration testing performed for the financial data run in PropWorks. The Airport performs backup recovery only when a file or a folder is lost or accidentally deleted but never tested the whole backup system. Whole backup testing needs to be done separately on a regular basis. Best practices suggest that disaster recovery plans should be tested at least once a year while simple backups should be tested much more frequently and whenever there is a major hardware or software change to the backup system.

Recommendation: We recommend that the Airport implement the best practices utilized in the industry and perform disaster recovery plan testing regularly. As much as possible, the test should duplicate the conditions DEN will face when data restore is actually needed, which means a complete restoration of all financial data to a second system with an identical configuration.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. DEN will develop formal Disaster Recovery Plans for the PropWorks IT Service. The testing of these Disaster Recovery Plans will be enforced by the 'compliance tasking' function that will be available in the aforementioned ServiceNow GRC module, which is pending capital funding.

Person(s) responsible for implementing: Cheryl Monroe, Director of Infrastructure and Operations.
Implementation date: December 31, 2018.

2017 D-11 The Airport New Hire Process

Finding: During our audit, we noted that a newly hired employee was granted access to the Airport's system before receiving the cybersecurity awareness training. For this same employee the Airport could not provide a signed user access agreement that was required to be signed before any user account is set up. Further, the Airport could not provide access approval document that shows the types of access assigned to this employee.

Recommendation: We recommend that the Airport should provide the cybersecurity awareness training to newly hired employees before they get access to the system to protect any unintentional vulnerability. Signed user access agreements should also be kept in a secured place accessible when needed.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. We will implement policy, technology, and processes which requires the successful completion of cybersecurity awareness training prior to network access being granted for all users.

Person(s) responsible for implementing: Tim Coogan, Chief Information Security Officer.
Implementation date: December 31, 2018.

2017 D-12 The Airport Full Access Privileges

Finding: Based on our review of the user access privileges, we noted that there were five IT employees who have been granted full access to all PropWorks modules and database administration. Our inquiry also confirms that IT employees have an ability to update customer files. Such access poses a risk as it gives the IT employee a right to modify and delete data from PropWorks.

Recommendation: We recommend that IT employees should not be granted full access in PropWorks and if that is necessary, a log should be maintained and reviewed by another person to track any changes they are making.

Views of Responsible Officials and Planned Corrective Actions: Although we agree with the observation, management feels that the compensating controls that are in place and working sufficiently reduce the residual risk to an acceptable level given the cost/benefit of deploying additional controls. No further remediation is planned.

Person(s) responsible for implementing: Not Applicable.
Implementation date: Not Applicable.

2017 D-13 The Airport Access to Data Centers

Finding: The Airport has a procedure of using badges or sign-in sheets (for un-badged) users for accessing the data centers. We requested a list of personnel authorized to physically access the data center, the sign-in sheet and access logs to the data centers during the month of December 2017. DEN, however, could not provide the access log and the sign-in sheet for our review. Also, DEN provided a global list of personnel with badges that does not identify the users who has a right to access the data centers.

Recommendation: We recommend that the Airport keep access logs to the data centers and sign-in sheet for unbadged visitors so that an independent person can review who has accessed the data centers. We also recommend the Airport maintain a list of individuals who have physical access privilege to the data center and regularly monitor logs.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. The Airport does keep access logs for the data center. The logs delivered during the audit did not include the month of December which was due to an error in the report. The data is now available upon request.

Additionally, although we agree with the observation that the Airport should maintain a list of individuals who have physical access privilege to the data center and regularly monitor logs, management feels that the compensating controls that are in place and working sufficiently reduce the residual risk to an acceptable level given the cost/benefit of deploying additional controls. No further remediation is planned.

Person(s) responsible for implementing: Cheryl Monroe, Director of Infrastructure and Operations.
Implementation date: Already Implemented.
We also observed matters that we consider to be deficiencies that we communicated to management orally.

INTERNAL CONTROL OVER COMPLIANCE

In planning and performing our audit, we considered City and County of Denver's (the City) internal control over compliance with the requirements that could have a direct and material effect on a major Federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with *OMB Uniform Guidance,* but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However as discussed below we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses, significant deficiencies and deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a Federal program on a timely basis.

A material weakness in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a Federal program will not be prevented or detected and corrected on a timely basis.

We observed the following matters that we consider to be material weaknesses, significant deficiencies or deficiencies:

MATERIAL WEAKNESSES

Refer to the Independent Auditor's Report on Compliance for Each Major Federal Program and on Internal Control Over Compliance.

SIGNIFICANT DEFICIENCIES

Refer to the Independent Auditor's Report on Compliance for Each Major Federal Program and on Internal Control Over Compliance.

DEFICIENCIES

2017 Single Audit D-1 Citywide – Uniform Guidance Procurement

Finding: The City implemented new procurement policies and procedures effective January 1, 2017 in order to conform to the Uniform Guidance requirements over Federal awards. While communication and training occurred prior to implementation, several departments seemed unclear about the new requirements indicating that additional training and education may be necessary. In addition, those departments that have direct purchasing authority and enter into multi-faceted contracts may need to implement additional policies and procedures to address some of the particular issues they face in procuring goods and services such as on-call contracts, continuation or phased contracts, etc. Further, while Uniform Guidance makes it clear that in certain circumstances pricing is not required to be the primary factor in the selection process, it does still require that some sort of price analysis be performed to ensure that pricing is reasonable. In many cases the City's support of this price analysis could be more formally documented and included in the procurement files.

Recommendation: We recommend that departments be reminded of the policies and procedures and the steps they must take to remain in compliance when purchases are below the threshold requiring formal involvement from the centralized purchasing department. In addition, departments with direct purchasing authority should be identified along with the complex procurement issues they each face in order to develop supplemental policies to address those needs. Finally, we recommend that tools for formally documenting price analysis during the procurement process be utilized and documentation be maintained in the procurement files.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. General Services Purchasing (GS) developed and issued in January 2017 an addendum to its overall policies and procedures. This addendum incorporates the policies and procedures that address the OMB Federal Uniform Procurement guidance requirements. This addendum was developed and issued in collaboration with the City Attorney's Office as a key part of the Federal

Uniform Guidance requirements are to include certain compliance provisions in City purchase orders and contracts that result from procurements.

The Federal Procurement Uniform guidance is directed to those procurement authorities in local and state governments that are responsible for sourcing vendors and contractors to provide goods and services for the benefit of local and state governments when utilizing Federal funds. In keeping with the mandate, GS Purchasing has aligned its policies and procedures to comply. By the end of the third quarter 2018, GS Purchasing will develop and deliver a guide for all city departments that will address their responsibilities and procedures that they need to be aware of and practice to be in compliance with the Federal Uniform Procurement Guidance requirements. GS Purchasing buyers will deliver and orient this guide to the departments they serve which will cover all departments.

The overarching requirement coming from the Federal Uniform Procurement Guidance is for non-Federal agencies (Cities and Counties) to align their procurement policies and procedures with the Federal Uniform Guidance so it is assured that procurements taking place are in compliance when there are Federal funds being the utilized. This has been accomplished by GS Purchasing for our scope of authority. Recognizing that certain City departments have their own procurement authority for construction and professional services, GS Purchasing has already met and shared our Policy and Procedures addendum with those departments. By the end of the third quarter 2018, GS Purchasing will provide guidance to these departments and assist them in developing their own policies and procedures to address compliance with the Federal Uniform Procurement Guidance requirements.

Ongoing — GS Purchasing will continue to periodically provide reinforcement of its Federal Uniform Procurement guidance policies to the City Grant Manager working group at its meetings.

Price/Cost Analysis — GS Purchasing, by the end of the third quarter 2018 will share its tools and methods it utilizes for complying with the price/cost analysis requirements including documentation.

Finally, GS Purchasing will work with the Mayor’s Office and the City Attorney’s Office to address revising Executive Order #8 (which provides certain services contracting authority for all City departments), so it reflects the applicable Federal Uniform Procurement guidance requirements for those procurements utilizing Federal funds.

Person(s) responsible for implementing: John Utterback, General Services Purchasing Manager.
Implementation date: September 30, 2018.

2017 Single Audit D-2 Citywide – Federal Grant Property and Equipment Management

Finding: During our testing and discussions with various departments within the City, we noted that per Fiscal Accountability Rule 9.2, each department is required to maintain and/or monitor an equipment and property inventory system to track purchased or received items under the grant. Per our review, we noted one or more of the below were missing from the property records provided by the Departments. Per 2 CFR Sections 200.313, the City must have property records which include:

- a description of the property
- the serial number or other identification number
- the source of funding for the property (including the Federal award identification number)
- title holder
- the acquisition date
- cost of the property
- percentage of Federal participation in the project costs for the Federal award under which the property was acquired
- the location of the property
- use and condition of the property
- any ultimate disposition data including the date of disposal and sales price of the property (2 CFR section 200.313(d)(1))

Recommendation: We recommend that the Workday Fixed Asset System be updated to include a field indicating if asset was purchased with Federal dollars. This will allow additional rules to be enabled within Workday for the missing requirements.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. A training was conducted by the Controller's Office in August of 2017 to inform agencies of the data elements that must be included within agency records for property purchased under a Federal grant. The Controller's Office will hold another training in 2018 to convey these requirements again. Additionally, the Controller's Office will update Fiscal Accountability Rule 9.2, Grant Management, to include the required data elements for property records and we will explore what additional fields can be utilized in Workday to better track this information.

Person(s) responsible for implementing: Shanna Tohill, Manager of Financial Reporting.
Implementation date: December 31, 2018.

2017 Single Audit-D-3 Citywide – Indirect Cost Rate

Finding: In accordance with 2 CFR 200.414 and Appendix VII, a governmental agency that receives more than $35 million in direct Federal funding must submit its indirect cost rate proposal to its cognizant agency for indirect costs. Prior to Uniform Guidance, the City had negotiated its indirect cost rate with the Colorado Department of Human Services (CDHS). Subsequently, CDHS informed the City that such authorization no longer fell within their authority and CDHS required the City utilize the 10% de minimis rate. We noted that certain departments are continuing to apply this old rate that is potentially no longer valid and may result in disallowed costs.

Recommendation: We recommend that the City evaluate the need to negotiate an indirect cost rate directly with their cognizant Federal Agency. Until such rate is negotiated, any use of an indirect cost rate above the de minimis 10% rate should be formally approved by the Federal Agency, documentation supporting such rate should be maintained, and the rate should be consistently applied to the Federal award for which it was approved.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. The Controller's Office will work with the City's Budget and Management Office to evaluate the need to negotiate a rate directly with our cognizant agency. Additionally, once it is determined what rate should be used by the City, the Controller's Office will coordinate the communication of the rate to be used Citywide.

Person(s) responsible for implementing: Shanna Tohill, Manager of Financial Reporting.
Implementation date: December 31, 2018.

2017 Single Audit D-4 Medicaid – Fraud Hotline

Finding: Any suspected fraud relating to the Denver Department of Human Services (DDHS) can be reported through either the City's general fraud hotline or through the DDHS Fraud Investigation Unit (the Unit). Once a fraud tip is received it is entered into WMS by the Unit. Primarily due to the volume of tips received, the first step of the Unit is to pass the information along to the appropriate division personnel to research and determine if a formal investigation is warranted. Normally, once a determination is reached by the division, the Unit is notified through a paper process, and the tracking system is updated triggering a formal investigation. During a period of staff turnover, a determination was reached by division personnel requiring a formal investigation, however, there was a failure in the paper process and the tip did not get updated in the tracking system and therefore further investigation was not performed.

Recommendation: We recommend that DDHS implement procedures to automate the fraud tip tracking process, perhaps by incorporating it into the already existing WMS system, to help ensure all fraud allegations are responded to and addressed timely.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. DDHS is currently working on a process where the investigation will be requested through WMS so the entire process can be tracked and monitored for accountability purposes. A stakeholder workgroup has been formed to address this and changes are being requested through our development team.

Person responsible for implementing: Richard Rogers, Denver Department of Human Services, Fraud Team Manager.
Implementation date: April 30, 2018.

We also observed matters that we consider to be deficiencies that we communicated to management orally.

OTHER MATTERS

Although not considered material weaknesses, significant deficiencies or deficiencies in internal control over financial reporting, we observed the following matters and offer these comments and suggestions with respect to matters which came to our attention during the course of the audit of the financial statements. Our audit procedures are designed primarily to enable us to form an opinion on the financial statements and, therefore, may not bring to light all weaknesses in policies and procedures that may exist. However, these matters are offered as constructive suggestions for the consideration of management as part of the ongoing process of modifying and improving financial and administrative practices and procedures. We can discuss these matters further at your convenience and may provide implementation assistance for changes or improvements.

2017 OM -1 HIV – Subrecipient Monitoring, Risk Assessments, and Management

Finding: In accordance with 2 CFR Section 200.331(b), pass through entities are required to evaluate each subrecipient's risk of noncompliance for purposes of determining the appropriate subrecipient monitoring. We noted that the Department's primary risk evaluation occurs during the competitive awarding process each year but is somewhat informal and not directly linked to monitoring activities. In addition, there may be a need or opportunity to utilize the onsite monitoring process to educate and assist subrecipient's in evaluating their own single audit requirements. Further, it was noted that the process for reimbursing subrecipients is very cumbersome to administer and requests are not being received timely adding to the complexities of administering this program.

Recommendation: We recommend that the Department develop a formal risk assessment document to be completed for each subrecipient within the respective award files. This documentation should include the items of consideration as described in 2 CFR 200.331(b). This risk assessment should result in a conclusion as to the level of monitoring required allowing program personnel to focus their monitoring and educational efforts on those subrecipients with the highest risk profile. In addition, we recommend that the risk assessment and onsite monitoring tools include an inquiry regarding the single audit requirements of each subrecipient so it is clearly documented if and when a single audit would be available for review. All single audits are available on the Federal audit clearinghouse which could be utilized for certain monitoring functions potentially creating efficiencies for both the City and its subrecipients. Further, we recommend that reimbursement guidelines surrounding timeliness be included in the award contracts and strict adherence should be encouraged.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding. The Denver Office of HIV Resources (DOHR) has begun a detailed review of existing policies and procedures and has identified area for improvement. DOHR staff, in conjunction with the Controller's Office staff, will review documentation requirements, meet to create and/or update policies, procedures and processes to ensure a more streamlined approach to complying with this requirement. DOHR will develop an Infrastructure Self-Assessment Questionnaire (ISAQ) to be completed by subrecipients that includes requirements detailed in Title 45 CFR Part 75, the Uniform Administrative Requirements, Cost Principles and Audit Requirement for HHS Awards. Policies, procedures, and processes will also include requirements for submission of audited financial statements and audit packages from the subrecipients along with due dates, review dates, and procedures for delinquent audit packages.

Person(s) responsible for implementing: Beau J. Mitts, Program Manager, HIV Resources.
Implementation Date: January 1, 2019.

2017 OM-2 HIV and AIP – Cash Management – Frequency of Drawdowns

Finding: During our testing of cash management for both the HIV and AIP programs, we noted that drawdown requests appear to be occurring infrequently resulting in very large drawdown requests and significant grants receivable balances throughout the year. This results in extended periods of time in which the City or DEN is covering the negative cash positions for these programs.

Recommendation: We recommend that the programmatic cash needs be evaluated on a monthly basis and drawdown requests be submitted more timely as appropriate in order to allow for more productive uses of City and DEN financial resources.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding.

Relative to HIV, the Denver Office of HIV Resources (DOHR) has begun a detailed review of existing policies and procedures and has identified area for improvement. Drawdown requests have historically been performed each calendar year quarter in alignment with the due date of the Federal Financial Report. DOHR staff, in conjunction with the Controller's Office staff, will review the drawdown requirements, meet to create and/or update policies, procedures and processes to ensure a more frequent drawdown. Requirements will include guidelines surrounding the timeliness of reimbursements within the award contracts.

Relative to DEN, during the audit period, DEN had some accounting staff transitions and were focused on testing and implementing the new general ledger system, Workday, that impacted the timeliness of the request for reimbursement. Toward the end of 2017, a new individual was assigned to the role of generating the drawdown request on the grants and is in continuous communication with the DEN project manager. Also, with the implementation of Workday, the grant module captures the costs to the vendor when paid and records the related grant revenues. Also, DEN has regularly scheduled monthly meetings between the project managers and the finance grant team to discuss status of the grants, including payments to vendors and billings.

Person(s) responsible for implementing: Beau J. Mitts, Program Manager, HIV Resources and Anne Bygrave, Fiscal Administrator, Controller's Office, Michael Biel, Senior Vice President of Financial Management.
Implementation Date: HIV – January 1, 2019, DEN – July 31, 2018.

2017 OM-3 New Accounting Pronouncements

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pension* (GASB 75)

GASB 75 replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB 75 requires governments to report a liability on the face of the financial statements in accordance with the following:

Employers that are responsible only for OPEB liabilities for 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 the assets accumulated in trust to make the benefit payments).

- Employers that participate in a cost-sharing OPEB plan that is administered through a trust that meets specified criteria will report a liability equal to the employer's proportionate share for the collective OPEB liability for all employers participating in the plan.

- Employers that do not provide OPEB through a trust that meets specified criteria will report the total OPEB liability for their own employees.

GASB 75 requires more extensive note disclosures and required supplementary information (RSI) about the OPEB liabilities. GASB 75 is effective for fiscal years beginning after June 15, 2017 and requires restatement of any prior years presented, if practical.

While GASB 75 is not effective until the City's fiscal year ending December 31, 2018, we recommend the City begin assessing the potential impact on the financial statements of this statement and begin the process of communicating this impact with those charged with governance and other stakeholders. Similar to the adoption of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions,* the adoption of GASB 75 will require advance coordination with plans and actuaries so that the required information is available.

GASB Statement No. 83, *Certain Asset Retirement Obligations*

GASB 83 addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement.
This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs. This Statement requires that recognition occur when the liability is both incurred and reasonably estimable. The determination of when the liability is incurred should be based on the occurrence of external laws, regulations, contracts, or court judgments, together with the occurrence of an internal event that obligates a government to perform asset retirement activities.

GASB 83 is effective for the City's fiscal year ending December 31, 2019. Earlier application is encouraged.

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.

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 December 31, 2019. Earlier application is encouraged.

GASB Statement No. 85, *Omnibus 2017*

The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). Specifically, this Statement addresses the following topics:

- Blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation
- Reporting amounts previously reported as goodwill and "negative" goodwill
- Classifying real estate held by insurance entities
- Measuring certain money market investments and participating interest-earning investment contracts at amortized cost
- Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus
- Recognizing on-behalf payments for pensions or OPEB in employer financial statements
- Presenting payroll-related measures in RSI for purposes of reporting by OPEB plans and employers that provide OPEB
- Classifying employer-paid member contributions for OPEB

- Simplifying certain aspects of the alternative measurement method for OPEB
- Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans

GASB 85 is effective for the City's fiscal year ending December 31, 2018. Earlier application is encouraged.

GASB Statement No. 87, *Leases*

In June 2017, GASB published Statement No. 87, *Leases*. This Statement was the result of a multi-year project to reexamine the accounting and financial reporting for leases. The new Statement establishes a single model for lease accounting based on the principle that leases represent the financing of the right to use an underlying asset. Specifically, GASB 87 includes the following accounting guidance for lessees and lessors:

Lessee Accounting**:** A lessee will recognize a liability measured at the present value of payments expected to be made for the lease term, and an intangible asset measured at the amount of the initial lease liability, plus any payments made to the lessor at or before the beginning of the lease and certain indirect costs. A lessee will reduce the liability as payments are made and recognize an outflow of resources for interest on the liability. The asset will be amortized by the lessee over the shorter of the lease term or the useful life of the asset.

Lessor Accounting**:** A lessor will recognize a receivable measured at the present value of the lease payments expected for the lease term and a deferred inflow of resources measured at the value of the lease receivable plus any payments received at or prior to the beginning of the lease that relate to future periods. The lessor will reduce the receivable as payments are received and recognize an inflow of resources from the deferred inflow of resources in a systematic and rational manner over the term of the lease. A lessor will not derecognize the asset underlying the lease. There is an exception for regulated leases for which certain criteria are met, such as airport-aeronautical agreements.

The lease term used to measure the asset or liability is based on the period in which the lessee has the noncancelable right to use the underlying asset. The lease term also contemplates any lease extension or termination option that is reasonably certain of being exercised.

GASB 87 does not apply to leases for intangible assets, biological assets (*i.e.* timber and living plants and animals), service concession agreements or leases in which the underlying asset is financed with conduit debt that is reported by the lessor. Additionally, leases with a maximum possible term of 12 months or less are excluded.

GASB 87 is effective for the City's fiscal year ending December 15, 2020. Early application is encouraged. It is anticipated that leases would be recognized using the facts and circumstances in effect at the beginning of the period of implementation.

GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*

GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements* (GASB 88). This Statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. This Statement also requires that existing and additional information be provided for direct borrowings and direct placements of debt separately from other debt.

GASB 88 is effective for the City's December 31, 2019 financial statements, with earlier application encouraged.

GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*

GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period* (GASB 89). This Statement improves financial reporting by providing users of the financial statements more relevant information about capital assets and the cost of borrowing for a reporting period. It will require that interest costs incurred before the end of a construction period be recognized as an expense in the period in which the costs is incurred. As a result, the interest cost incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type or enterprise fund.
GASB 89 is effective for the City's December 31, 2020 financial statements, with earlier application encouraged.

While several of these standards are not effective in the short-term, we recommend the City begin assessing the potential impact on the financial statements of all of these statements and begin the process of communicating this impact with those charged with governance and other stakeholders.

Management's written response to the deficiencies, significant deficiencies, and material weaknesses identified in our audit has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

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

BKD, LLP

June 5, 2018