

**CITY OF MCKINNEY, TEXAS**

**FEDERAL SINGLE AUDIT REPORTS**

**YEAR ENDED SEPTEMBER 30, 2012**

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**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON  
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING  
STANDARDS**

The Honorable Mayor and City Council  
City of McKinney, Texas

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of City of McKinney, Texas (the City), as of and for the year ended September 30, 2012, which collectively comprise the City's basic financial statements and have issued our report thereon dated March 1, 2013. We conducted our audit 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.

Internal Control Over Financial Reporting

Management of the City is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as previously defined. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting [12-01, 12-02, and 12-03]. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention of City Council.

City of McKinney, Texas

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The City's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of audit committee, management, City Council, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Weaver and Tidwell LLP*

WEAVER AND TIDWELL, L.L.P.

Dallas, Texas  
March 1, 2013



**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR  
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE  
WITH OMB CIRCULAR A-133**

The Honorable Mayor and City Council  
City of McKinney, Texas

Compliance

We have audited the City of McKinney, Texas (the City)'s compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended September 30, 2012. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2012.

Internal Control Over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the 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 Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

*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 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.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

#### Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, business-type activities, the aggregate discretely presented component units, each major fund and the aggregate remaining fund information of the City of McKinney as of and for the year ended September 30, 2012 and have issued our report dated March 1, 2013. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the City of McKinney's financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audits of State, Local Governments, and Non-Profit Organizations, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

City of McKinney, Texas

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The purpose of this report is solely to describe the scope of our testing of compliance with the types of compliance requirements applicable to each of the City's major programs and our testing of internal control over compliance and the results of our testing, and to provide an opinion on the City's compliance but not provide an opinion on the effectiveness of the City's internal control over compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the City's compliance with requirements applicable to each major program and its internal control over compliance. Accordingly, this report is not suitable for any other purpose.

*Weaver and Tidwell LLP*

WEAVER AND TIDWELL, L.L.P

Dallas, Texas  
March 1, 2013

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**I. Summary of the Auditor's Results:**

Financial Statements

- a. An unqualified opinion was issued on the financial statements.
- b. Internal control over financial reporting:
  - Material weakness(es) identified? \_\_\_\_\_ Yes      X   No
  - Significant deficiency(ies) identified that are not considered a material weakness? \_\_\_\_\_   X   Yes    \_\_\_\_\_ No
- c. Noncompliance material to financial statements noted \_\_\_\_\_ Yes      X   No

Major Programs

- d. Internal control over major programs:
  - Material weakness(es) identified? \_\_\_\_\_ Yes      X   No
  - Significant deficiency (ies) identified that are not considered a material weakness? \_\_\_\_\_ Yes      X   None reported
- e. An unqualified opinion was issued on compliance for major programs.
- f. Any audit findings disclosed that were required to be reported under Section 510(a) or OMB Circular
  - A-133. \_\_\_\_\_ Yes      X   No

g. Identification of major programs:

Program/Cluster Name	CFDA #
Airport Improvement Program	20.106
Energy Efficiency & Conservation Block Grant - ARRA	81.128



**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

- h. The dollar threshold used to distinguish between type A and type B programs. \$419,680
- i. Auditee qualified as a low-risk auditee.  Yes  No

**II. Findings Relating to the Financial Statements Which Are Required To Be Reported in Accordance with *Generally Accepted Government Auditing Standards*.**

**Finding 12-01 Recognition of a Non Cash Transaction**

Type: Financial reporting and disclosure finding.

Criteria: Capital assets or other nonfinancial resources should be recorded when received.

Condition: Capital assets deeded to McKinney Community Development Corporation (MCDC) as part of an economic agreement or settlement was not recorded.

Context: Land and land improvements deeded to MCDC during the 2011 fiscal year as part of a lawsuit settlement related to an economic development agreement with a fair value of \$7,052,564 was not recorded in the year received.

Cause: The City's Finance Department was not aware that the assets had been deeded to MCDC as part of the settlement due to insufficient controls and accounting procedures related to non cash transactions.

Effect: Capital assets for discretely presented component units were understated by \$7,052,564.

Recommendation: The City should implement controls and procedures to ensure that agreements having financial statement implications be provided to the Finance Department.

Management Response: When the transaction took place in 2011 it was presented that MCDC acquired ownership of TBG. It was not discovered until current management and MCDC staff began reconciling assets and determined the TBG transaction included acquiring ownership of real property at the Gateway site.

The current Financial Services staff, including the CFO, has increased correspondence with legal, city and component unit management as well as Board members by attending monthly meetings and staying abreast of economic agreements and other projects resulting in cash and non-cash financial transactions. In addition, we have assigned a Senior Accountant to review and monitor all component unit financial transactions ensuring more accurate reporting.

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**Finding 12-02 Funds Received and Expended by an Agent on Behalf of the City**

Type: Financial reporting and disclosure finding.

Criteria: Funds received and expended by an agent on behalf of the City should be reflected in the financial statements

Condition: Capital assets purchased by the Texas Department of Transportation, acting as the agent on the project, on behalf of the Collin County Airport Development Corporation (CCADC) was not recorded.

Context: Capital assets of 6% of the aggregate CCADC capital assets and revenues of 32% of the aggregate CCADC revenues were not recorded as of 2011 fiscal year end.

Cause: The City had not been made aware of the expenditures administered by the Texas Department of Transportation until the 2012 fiscal year due to insufficient controls and accounting procedures related to non cash transactions.

Effect: Capital assets for discretely presented component units were understated by \$3,712,990.

Recommendation: The City should implement controls and procedures to ensure that funds received and expended by an agent acting on behalf of the City are reconciled and recorded in the year the expenditures are incurred.

Management Response: Texas Department of Transportation – Aviation Division handles all FAA funds received and expended for airport related projects. The City of McKinney receives regular updates from TxDOT on project status and payments made on behalf of the City. Financial Services staff conducted a comprehensive audit of all CCADC grants and CIP projects. Staff identified a grant in which TxDOT Aviation had not reported any expenditures. Upon research, it was determined that TxDOT Aviation was not handling the construction contract for the relocation of FM 546 as part of the CCADC's replacement runway project. Unbeknownst to the City, TxDOT's Transportation Division was responsible for this contract and was not providing Financial Services staff with expenditures related to the contract.

In the future, the City will establish unique project numbers for CIP related grant awards. In addition, all grant awards received and expended by an agent on behalf of the City will be audited and reported quarterly in the Grants Report. This will include Financial Services staff directly contacting any agent(s) receiving and expending funds on behalf of the City for reconciliation purposes.

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**Finding 12-03    Recording of Infrastructure**

Type: Financial reporting and disclosure finding.

Criteria: Capital assets should be recorded by the City if the assets are deemed to be the property of the City.

Condition: Capital assets of another governmental entity were recorded as capital assets by the City.

Context: Capital assets of another governmental entity in the amount of \$7,578,461 were improperly recorded as infrastructure construction in progress by the City in previous fiscal years.

Cause: The City was not aware that the assets would not be maintained by the City due to insufficient controls and accounting procedures or processes over capital asset reporting.

Effect: Capital assets of the City's governmental activities were overstated by \$7,578,461.

Recommendation: The City should implement controls and procedures to ensure that infrastructure is recorded for assets constructed and/or contributed to the City, if and only if, the infrastructure qualifies as an asset of the City in accordance with generally accepted accounting principles.

Management Response: The City of McKinney constructs on behalf of or participates with other entities in the construction of infrastructure within the city. In some instances our CIP projects are State or County owned infrastructure. The City's new Senior CIP Accountant performed an audit of our capital improvements program and identified construction in progress that was recorded as City infrastructure that was state or county owned infrastructure. For example, Custer Road, US 75 and Hwy 5 improvements were City funded CIP projects but are State or County owned infrastructure.

The Senior CIP Accountant will continue to monitor and audit all projects for proper capital asset recording. This will include coordinating with Development Services/Engineering to identify all projects that are not City owned infrastructure.

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**III. Findings and Questioned Costs for Federal Awards Including Audit Findings as  
Described in I.f Above**

**NONE**

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**IV. Summary of Prior year Findings.**

**None**

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

	<u>CFDA Number</u>	<u>Grant Number</u>	<u>Expenditures</u>
<b>U.S. DEPARTMENT OF ENERGY</b>			
Direct Funding			
Energy Efficiency and Conservation Block Grant - ARRA	81.128	SC0001875	\$ 401,021
Passed through the State Energy Conservation Office			
State Energy Program - Solar Array Fire Station #6 - ARRA	81.041	DE-EE000116	<u>55,433</u>
<b>TOTAL U.S. DEPARTMENT OF ENERGY</b>			<u>456,454</u>
<b>U.S. ENVIRONMENTAL PROTECTION AGENCY</b>			
Direct Funding			
Brownfield Hazardous	66.818	BF-00F16601-0	54,226
Brownfield Petroleum	66.818	BF-00F16201-0	<u>36,484</u>
<b>TOTAL U.S. ENVIRONMENTAL PROTECTION AGENCY</b>			<u>90,710</u>
<b>U.S. DEPARTMENT OF JUSTICE</b>			
Passed through the City of Plano			
Justice Assistance Program	16.738	2010-DJ-BX-1029	10,358
Direct Funding			
Bullet Proof Vest Reimbursement	16.607	n/a	<u>10,642</u>
<b>TOTAL DEPARTMENT OF JUSTICE</b>			<u>21,000</u>
<b>U.S. DEPARTMENT OF TRANSPORTATION</b>			
Direct Funding			
FAA Grant - Replacement Runway	20.106	8XXAV038	<u>12,825,955</u>
<b>TOTAL U.S. DEPARTMENT OF TRANSPORTATION</b>			<u>12,825,955</u>
Direct Funding			
Urban Area Security Initiative (UASI)	97.008	2010-SS-T0-0008	11,304
Urban Area Security Initiative (UASI)	97.008	2010-SS-0008	<u>5,000</u>
<b>TOTAL U.S. DEPARTMENT OF HOMELAND SECURITY</b>			<u>16,304</u>
<b>U.S. DEPARTMENT OF AGRICULTURE</b>			
Direct Funding			
Rehabilitation of 1A, 2B & 17 - Watershed Protection and Flood Prevention - ARRA	10.904	69-7442-5-709	<u>67,853</u>
<b>TOTAL U.S. DEPARTMENT OF AGRICULTURE</b>			<u>67,853</u>
<b>U.S. DEPARTMENT OF HOUSING &amp; URBAN DEVELOPMENT</b>			
Direct Funding			
Community Development Block Grant	14.218	B-10-MC-48-0043	413,694
Community Development Block Grant-ARRA	14.253	B-09-MY-48-0043	<u>5,301</u>
Total CDBG - Entitlement Grants Cluster			418,995
Homebuyer Assistance	14.239	M-09-SG-48-0100/1001333	<u>92,059</u>
<b>TOTAL U.S. DEPARTMENT OF HOUSING &amp; URBAN DEVELOPMENT</b>			<u>511,054</u>
<b>TOTAL EXPENDITURES</b>			<u>\$ 13,989,330</u>

**CITY OF MCKINNEY, TEXAS  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED SEPTEMBER 30, 2012**

**1. GENERAL**

The accompanying schedule of expenditures of federal awards presents the activity of all applicable federal awards of the City of McKinney, Texas (the City). The City's reporting entity is defined in Note 1 to the City's basic financial statements.

**2. BASIS OF ACCOUNTING**

The accompanying schedule of expenditures of federal awards is presented using modified accrual basis of accounting, which is described in Note 1 to the City's basic financial statements. Grants are generally accounted for in special revenue funds, except for the FAA grants, which are recorded in the Collin County Airport Development Corporation, a discretely presented component unit which is accounted for as an enterprising activity.

**3. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS**

Amounts reported in the accompanying schedule may not agree with amounts reported in the related federal financial reports since the City used the modified accrual basis of accounting in preparing the schedule and the cash basis in preparing the federal financial reports.

**4. CONTINGENCIES**

The City participates in several grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by grantor agencies. Therefore, to the extent that the City has not complied with the rules and regulations governing the grants, refunds of any money received may be required, and the collectability of any related receivable at September 30, 2012 may be impaired. In the opinion of the management, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants.