

SHAREHOLDERS:
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Armstrong, Vaughan & Associates, P.C.
Certified Public Accountants

Communication with Those Charged with Governance

February 17, 2017

To the Council
City of Balcones Heights

We have audited the financial statements of the City of Balcones Heights, for the year ended September 30, 2016, and have issued our report thereon dated February 17, 2017. Professional standards require that we advise you of the following matters related to our audit.

Our Responsibility in Relation to the Financial Statement Audit

As communicated in our engagement letter dated July 15, 2016, our responsibility as described by professional standards, is to form and express an opinion about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material aspects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control over financial reporting. Accordingly, as part of our audit, we considered the internal control of City of Balcones Heights solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

Planned Scope and Timing of the Audit

We conducted our audit consistent with the planned scope and timing we previously communicated to you.

Compliance with All Ethical Requirements Regarding Independence

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

Qualitative Aspects of the Entity's Significant Accounting Practices

Significant Accounting Policies

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by the City are described in Note A to the financial statements. There have been no initial selection of accounting policies and no changes in significant accounting policies or their application during 2016. No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

Significant Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgments. The most sensitive estimate affecting the financial statements was:

- Management's estimate of useful lives of capital assets is based on published industry guidance and professional judgment.
- Net Pension Liability assumptions for mortality rates and investment returns are based on the actuarial study performed by Texas Municipal Retirement System with no input from the City's management.

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

Financial Statement Disclosures

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive financial statement disclosure includes employees' retirement systems.

Significant Difficulties Encountered during the Audit

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

Uncorrected and Corrected Misstatements

For purposes of this communication, professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that we believe are trivial, and communicate them to the appropriate level of management. Further, professional standards require us to also communicate the effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole and each applicable opinion unit. Management has corrected all identified misstatements.

In addition, professional standards require us to communicate to you all material, corrected misstatements that were brought to the attention of management as a result of our audit procedures. The following misstatement that we identified as a result of our audit procedures was brought to the attention of, and corrected by, management:

1. Corrected the expenditures related to the grant funds and city match portion of capital projects.
2. Corrected balance showing as retirement payable as of year-end.

We also assisted management with routine year-end accruals. We did not consider the adjustments to be significant deficiencies in controls.

Disagreements with Management

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

Representations Requested from Management

We have requested certain representations from management that are included in the management representation letter dated February 17, 2017.

Management Consultations with Other Independent Accountants

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

Other Significant Matters, Findings, or Issues

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

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Compliance with Public Funds Investment Act

The Public Funds Investment Act, (the "Act") requires that we include, as part of our audit, procedures to determine if the City of Balcones Heights had complied with the provisions of the Act. We found the City had complied, in all material respects, with the provisions of the Act.

Trend Analysis

We have prepared the attached "Trend Analysis" as a financial planning tool for council and staff. Sound financial management dictates that a minimum fund balance be maintained that is sufficient to ensure operations will continue uninterrupted and emergencies that arise from time to time will be met. A rule of thumb for a minimum fund balance for the general fund is three to six months average operating expenditures (exclusive of capital outlay and debt service expenditures). The attachment details the trends over the last six years. This is presented for additional analysis and as a planning tool. We make no recommendation regarding the analysis of this information.

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

A handwritten signature in cursive script that reads "Armstrong, Vaughan & Associates, P.C.".

Armstrong, Vaughan & Assoc., P.C.

February 17, 2017

CITY OF BALCONES HEIGHTS

TREND ANALYSIS

	09-30-11	09-30-12	09-30-13	09-30-14	09-30-15	09-30-16
FUND BALANCE - GENERAL FUND (Unassigned)	\$ 1,114,991	\$ 1,257,853	\$ 1,484,473	\$ 1,221,475	\$ 1,443,011	\$ 1,019,689
AVERAGE MONTHLY OPERATING EXPENDITURES (1)	\$ 326,745	\$ 351,969	\$ 356,171	\$ 361,512	\$ 387,913	\$ 339,540
GROWTH RATE PER YEAR - AVERAGE MONTHLY OPERATING EXPENDITURES	13.8%	7.8%	1.2%	1.5%	7.3%	-12.5%
# MONTHS AVERAGE EXPENDITURES IN RESERVE	3.4	3.6	4.2	3.4	3.7	3.0
FUND BALANCE - ALL GOVERNMENTAL FUND TYPES (2)	\$ 3,777,100	\$ 3,503,310	\$ 4,206,561	\$ 3,765,936	\$ 4,185,533	\$ 4,274,398
GENERAL BONDED DEBT	\$ 1,336,000	\$ 1,043,000	\$ 741,000	\$ 429,000	\$ 374,000	\$ 317,000
RATIO OF FUND EQUITY TO BONDED DEBT	2.8/1	3.4/1	5.7/1	8.8/1	11.2/1	13.5/1
NET POSITION (3)	\$ 159,008	\$ 143,085	\$ 90,517	\$ 76,047	\$ 58,250	\$ 136,556

(1) Exclusive of Capital and Debt Service Expenditures

(2) Includes General, Special Revenue, Debt Service and Capital Projects Funds (exclusive of encumbrances)

(3) Includes Sewer O&M and Stormwater.