



Management Letter

February 26, 2015

To the Honorable Mayor and
City Council Members of the
City of Mont Belvieu, Texas:

The American Institute of Certified Public Accountants (Statement on Auditing Standards No. 115, *Communicating Internal Control Related Matters Identified in an Audit*, "SAS 115") provides guidance to auditors on communicating internal control matters to management and the governing body, board of directors, or equivalent body.

It is important to note when reviewing findings reported within this letter that classification of the findings is based on the definitions required by SAS 115 as further discussed below. Please note that these classifications are based on the potential impact to the financial statements, not necessarily the likelihood of actual loss to the City. Accordingly, the City's assessment of the "significance" or ranking of severity will likely be substantially different based on a number of factors including, but not limited to, its assessment of risk and the cost benefit of making the change.

Our report is as follows:

In planning and performing our audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Mont Belvieu, Texas (the "City") as of and for the year ended September 30, 2014, 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 opinions 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 material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be other matters.

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 City's financial statements will not be prevented, or detected and corrected, on a timely basis.

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A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our findings and additional comments are as follows:

Other Matters:

2014.001. GASB STATEMENT NO. 68, ACCOUNTING AND FINANCIAL REPORTING FOR PENSIONS

Background

In 2015, all local governments will begin to report their pension liability on their financial statements resulting in some governments reporting deficit equity positions. As some governments' pension liability becomes front page news, it is likely that pension liability will move to the arena of public discussions and, accordingly, elected and appointed officials need to be prepared to be familiar with key talking points, as noted in the recommendations below.

In June 2012, the Governmental Accounting Standards Board (GASB) issued Statement No. 68 ("GASB 68"), *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, which replaces the requirements of GASB Statement No. 27, as well as the requirements of GASB Statement No. 50, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements. GASB 68 will be effective for fiscal years beginning after June 15, 2014. The requirements of GASB Statement Nos. 27 and 50 will remain applicable for pensions that are not covered by the scope of GASB 68.

GASB 68 establishes new standards of accounting and financial reporting for defined benefit and defined contribution pensions provided to the employees of state and local governmental employers. This statement establishes new standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures, in addition to new disclosure and Required Supplementary Information reporting requirements. Implementation of GASB 68 will represent a significant change in the accounting and reporting of pension expense and the related liability. For fiscal year 2015, the City will be required to recognize its long-term obligation for pension benefits as a liability in its government-wide statements.

Key changes to financial reporting and disclosures required by GASB 68 are as follows:

- A net pension liability (unfunded accrued liability) will be recognized on the Statement of Net Position. Previously this was a note disclosure only.
- This liability amount being reported will likely be higher than the amount previously disclosed, as the following changes will impact the calculation:
- Changes in the allowable amortization periods will result in larger expenses than previously reported.
- Previous statements provided up to six allowable actuarial cost methods. GASB 68 will require the use of only the entry age normal cost method.

- Previous standards allowed various asset smoothing methods to determine the values of plan assets. GASB 68 will require plan assets to be reported at fair market value.
- New terminology (net pension liability and total pension liability) will be used.
- Pension expenses will become more variable.
- More extensive disclosures and Required Supplementary Information will be included.

Key changes to the City's operations as a result of GASB 68 are as follows:

- Management will now be responsible documenting and taking responsibility for controls related to employee data being transmitted to its pension plan administrator.
- The City's independent auditor will now be required to review and test controls related to employee data being transmitted to the pension plan administrator.

Recommendation

Key talking points that management and elected officials should consider are:

1. The fundamentals of the government's finances have not changed.
2. This is an accounting rule change only.
3. Pension liability is a long-term liability paid off in the future.
4. The City is a member of Texas Municipal Retirement System (TMRS) and has made the necessary annual contributions as calculated by TMRS' actuary.
5. Fund balance remains the best measure of the financial health of a government.

As a result of this new accounting statement, it is important that management has reviewed and documented its internal controls over pension benefits. Internal controls should include various activities over pension benefits, such as plan design and modifications, employee eligibility, employee and employer contributions, reporting, and application for plan benefits. In addition, it is the employer's responsibility for ensuring the reasonableness of its pension liability. Factors to be considered in determining reasonableness include reviewing evidence used in determining the total pension liability such as assumptions made and completeness of the census data provided to the actuary. Possible procedures to ensure accuracy of the census data could include tracing active employees from payroll records to census data and checking key information, tracing current year terminations per payroll records to census data to verify status and date of termination, and tracing key data from the census file back to originating employment records.

TMRS will be providing the City with the information necessary to report its total pension liability and related disclosures. TMRS is anticipating this information will be available to cities in June 2015 via the City Portal. If the City has not already signed up for access to TMRS resources on the City Portal, it is highly recommended to do so. More information on this can be found at http://www.tmr.com/city_portal.php.

Additional resources can be found on our website, www.texasauditors.com, as well as <http://www.gasb.org/jsp/GASB/Page/GASBSectionPage&cid=1176163527940> where GASB has provided an implementation toolkit for governments. Additionally, we will send out client alerts as additional information becomes available on this topic.

2014.002. DEFICIT FUND BALANCE

Finding

As disclosed in the notes to the financial statements, the 2010 general obligation construction projects fund had an ending deficit fund balance.

Recommendation

The City should monitor expenditures related to construction projects or other special projects and budget for transfers in as necessary to cover the expenditures in these funds.

2014.003. AVAILABILITY OF COUNCIL MEETING MINUTES

Finding

It was discovered during the audit that council meeting minutes were not readily available for review.

Recommendation

The council should adopt policies that ensure the minutes are available for review by the public. The policy should include a timeline for the posting and availability of minutes.

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

We would like to thank the City Council and the City's management for their cooperation during the course of our audit. Please feel free to contact us at your convenience to discuss this report or any other concerns that you may have.

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