

# AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type: <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name: <u>City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust</u>	County Oakland
Audit Date December 31, 2003	Opinion Date April 30, 2004	Date Accountant Report Submitted To State: June 14, 2004	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations.

You must check the applicable box for each item below:

- |   |   |
|---|---|
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.   |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).  |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).  |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.   |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91] or P.A. 55 of 1982, as amended [MCL 38.1132])   |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.   |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).   |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).  |

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reports on individual federal assistance programs (program audits).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Single Audit Reports (ASLGU).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>

Certified Public Accountant (Firm Name): <b>Plante &amp; Moran, PLLC</b>			
Street Address 27400 Northwestern Highway	City Southfield	State MI	ZIP 48034
Accountant Signature  <i>Plante &amp; Moran, PLLC</i>			

**City of Pontiac**  
**Police and Fire Retiree Prefunded**  
**Group Health and Insurance Trust**

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**Financial Report**  
**December 31, 2003**

# **City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust**

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## **Contents**

<b>Report Letter</b>	1
<b>Management's Discussion and Analysis</b>	2-3
<b>Basic Financial Statements</b>	
Statement of Trust Net Assets	4
Statement of Changes in Trust Net Assets	5
Notes to Financial Statements	6-7



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## Independent Auditor's Report

To the Board of Trustees  
Police and Fire Retiree Prefunded  
Group Health and Insurance Trust

We have audited the accompanying statement of trust net assets of the City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust (a component unit of the City of Pontiac, Michigan) as of December 31, 2003 and the related statement of changes in trust net assets for the year then ended. These financial statements are the responsibility of the Board of Trustees of the Police and Fire Retiree Prefunded Group Health and Insurance Trust of the City of Pontiac. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust as of December 31, 2003 and the results of its operations for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis (identified in the table of contents) is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

*Plante & Moran, PLLC*

April 30, 2004

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# City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust

## Management's Discussion and Analysis

### Using this Annual Report

This annual report consists of two parts: (1) management's discussion and analysis (this section), and (2) the basic financial statements. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

### Condensed Financial Information

The table below compares key financial information in a condensed format between the current year and the prior year:

	Fiscal Year Ended December 31	
	2003	2002
Total assets	\$ 16,188,053	\$ 9,428,907
Total liabilities	<u>1,614,100</u>	<u>143,770</u>
Net trust assets	<u><b>\$ 14,573,953</b></u>	<u><b>\$ 9,285,137</b></u>
Net investment gain (loss)	\$ 3,566,789	\$ (1,743,469)
Contributions - Employer	3,113,968	2,575,510
Retiree health benefits paid	<u>1,363,688</u>	<u>637,107</u>
Contributions in excess of benefits paid	1,750,280	1,938,403
Ratio of contributions to benefits paid	228.3%	404.3%
General and administrative expenses	<u>28,253</u>	<u>5,135</u>
Net increase in trust net assets	<u><b>\$ 5,288,816</b></u>	<u><b>\$ 189,799</b></u>

# **City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust**

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## **Management's Discussion and Analysis (Continued)**

### **Overall Fund Structure and Objectives**

The Police and Fire Retiree Prefunded Group Health and Insurance Trust (the "Trust") exists to pay health care benefits to members retiring on or after August 22, 1996. Benefits currently being paid are significantly less than contributions currently being received. The excess of contributions over benefits paid will allow for additional funding to increase investment income to a level where the Trust will generate adequate earnings to pay future benefits. The public capital markets represent the primary source of investments.

### **Asset Allocation**

The Police and Fire Retiree Prefunded Group Health and Insurance Trust has established asset allocation policies, which are expected to deliver more than enough investment income over a very long period of time to satisfy the obligations to pay the benefits promised to the members of the Trust. The following are the asset allocation targets as of December 31, 2003:

Domestic equities	65%
International equities	15%
Domestic fixed income	20%

### **Investment Results**

The investment performance showed a marked improvement from the past three years of a highly challenging period in the capital markets. The stock market, as measured by the S&P 500 index, returned 28.7 percent as compared to the prior year at a negative 22 percent. The Trust experienced a healthy gain on its investment portfolios owing primarily to the improvement in the market value of stocks. Returns from fixed income investments declined to historic lows in the summer of 2003 due in large part to Federal Reserve monetary policy and remained slightly positive. The net assets of the fund increased by \$5,288,816 for the year.

While this year's fund investment return is significantly better than the prior year, it must be considered in a longer-term context. The asset allocation of each fund is built upon the foundation that the obligations of the Trust to pay the benefits promised to members and retirees are very long-term obligations. Accordingly, the Board of Trustees must make investment decisions that it believes will be the most beneficial to the Trust over many years, not just one or two years.



**City of Pontiac  
Police and Fire Retiree Prefunded  
Group Health and Insurance Trust**

**Statement of Changes in Trust Net Assets  
Year Ended December 31, 2003**

**Additions**

Investment income:

Interest and dividend income	\$ 249,600
Net appreciation in fair value of investments	3,342,189
Investment advisor fees	<u>(25,000)</u>

Net investment income 3,566,789

Contributions - Employer 3,113,968

Total additions 6,680,757

**Deductions**

Retirees' health benefits	1,363,688
Other expenses	<u>28,253</u>

Total deductions 1,391,941

**Net Increase in Trust Net Assets** 5,288,816

**Trust Net Assets - January 1, 2003** 9,285,137

**Trust Net Assets - December 31, 2003** \$ 14,573,953

# **City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust**

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**Notes to Financial Statements  
December 31, 2003**

## **Note 1 - Summary of Significant Accounting Policies**

The City of Pontiac (the "City") has established an irrevocable prefunded group health and insurance trust fund (the "Trust") for health, optical, dental, and life insurance benefits for retirees who are members of the Police and Fire Retirement System of the City of Pontiac, and who retired on or after August 22, 1996. The Trust was created as an Internal Revenue Code 501(c)(9) Trust (VEBA). The Police and Fire Retirement System (the "Retirement System") performs the Trust's accounting function.

**Reporting Entity** - The Trust is a component unit of the City of Pontiac, Michigan. The Trust does not hold securities of or loans to the City or Police and Fire Retirement System.

**Basis of Accounting** - The City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust's statements are prepared using the accrual basis of accounting. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Insurance costs are recognized when due and payable in accordance with the terms of the Trust.

**Investments** - Investments are reported at fair value. Money market funds and mutual fund investments are valued at net asset value. Dividend income is recorded on the ex-dividend date. Income from other investments is recorded as earned on an accrual basis. In accordance with the policy of stating investments at fair value, net unrealized appreciation or depreciation for the year is reflected in the statement of changes in trust net assets.

**Federal Income Taxes** - The Trust is exempt from income tax under Section 501(a).

## **Note 2 - Investments**

At December 31, 2003, investments consisted solely of money market accounts and mutual funds. The mutual funds are registered with the SEC. Investments are normally categorized to give an indication of the level of risk assumed by the Trust; however, money market accounts and mutual funds are not categorized because they are not evidenced by securities that exist in physical or book entry form.

# **City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust**

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**Notes to Financial Statements  
December 31, 2003**

## **Note 3 - Trust Contribution Information**

The Trust is funded by employer contributions. During the current year, an actuarial valuation was performed and the required employer-contribution rate was changed from 19.14 percent to 21.49 percent of police and fire wages effective July 1, 2003.

## **Note 4 - Trustees**

The trustees of the City of Pontiac Police and Fire Retiree Prefunded Group Health and Insurance Trust as of December 31, 2003 were appointed by the City of Pontiac Police and Fire Retirement System and the City of Pontiac.