

AUDITING PROCEDURES REPORT

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

Local Government Type: <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name: <u>City of Warren Police and Fire Retirement Systems, Michigan</u>	County Macomb
Audit Date 12/31/2003	Opinion Date May 19, 2004	Date Accountant Report Submitted To State:	

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 type="checkbox"/>	<input type="checkbox"/>	<input checked="" 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): PLANTE & MORAN, PLLC			
Street Address 27400 Northwestern Highway	City Southfield	State MI	ZIP 48037
Accountant Signature <i>Plante & Moran, PLLC</i>			

City of Warren Police and Fire Retirement System

**Financial Report
with Supplementary Information
December 31, 2003**

City of Warren Police and Fire Retirement System

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Independent Auditor's Report

To the Retirement Commission
City of Warren Police and Fire
Retirement System
City of Warren, Michigan

We have audited the accompanying basic financial statements of the City of Warren Police and Fire Retirement System (a component unit of the City of Warren, Michigan) as of and for the year ended December 31, 2003, as listed in the table of contents. These financial statements are the responsibility of the Police and Fire Retirement Commission of the City of Warren. 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 plan net assets of the City of Warren Police and Fire Retirement System as of December 31, 2003 and the changes in plan net assets for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the schedules of funding progress and employer contributions, as identified in the table of contents, are not a required part of the basic financial statements but are 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

May 19, 2004

City of Warren Police and Fire Retirement System

Management's Discussion and Analysis

Using This Annual Report

This annual report consists of three parts: (1) management's discussion and analysis (this section), (2) the basic financial statements, and (3) required supplementary information. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The basic financial statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Condensed Financial Information

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

	<u>Fiscal Year Ended December 31, 2003</u>	<u>Fiscal Year Ended December 31, 2002</u>
Total assets	\$ 297,017,665	\$ 260,945,567
Total liabilities*	<u>31,444,419</u>	<u>30,206,571</u>
Net assets held in trust for pension benefits	<u>\$ 265,573,246</u>	<u>\$ 230,738,996</u>
Net investment gain (loss)*	\$ 48,011,743	\$ (34,186,079)
Contributions:		
Employee	375,025	327,008
Employer	149,553	2,573,066
Employer contributions made on behalf of employees	1,148,042	1,131,726
Retiree pension and annuity benefits	13,772,426	13,046,229
Member refunds and annuity withdrawals	848,659	641,199
Benefits paid in excess of contributions	12,948,465	9,655,628
Ratio of benefits paid to contributions	8.74	3.39
General and administrative expenses	229,028	239,702
Net increase (decrease) in net assets held in trust	34,834,250	(44,081,409)

* Includes securities lending transactions

City of Warren Police and Fire Retirement System

Management's Discussion and Analysis (Continued)

Overall Fund Structure and Objectives

The City of Warren Police and Fire Retirement System (the "System") exists to pay benefits to its members and retirees. Active members earn service credit that entitles them to receive benefits in the future. Benefits currently being paid are significantly greater than contributions currently being received. The excess of benefits over contributions must be funded through investment income. The public capital markets represent the primary source of investments.

Asset Allocation

The System 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 System. The following is a summary of the actual asset allocations as of December 31, 2003:

Real estate investment trusts	3%
Large cap domestic equities	42%
Small cap domestic equities	14%
International equities	11%
Fixed income securities	28%
Cash	2%

Investment Results

The System experienced a recovery this past year after three demanding and challenging years in the capital markets. The stock market, as measured by the S&P 500, rose 28.7 percent and the Russel 2000 rose 47.3 percent. The Lehman Brothers Government/Corporate Index rose 4.7 percent. A significant gain of 41.4 percent was earned from the real estate investment trust portfolio. Overall, the system experienced sizeable gains in all asset categories.

While this year's total fund investment return exceeded actuarial expectations, it must be considered in a long-term context. The asset allocation of the fund is built upon the foundation that the obligations of the System 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 System over many years, not just one or two years.

Contacting the System's Management

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the System's finances and to show the System's accountability for the money it receives. If you have questions about this report or need additional information, we welcome you to contact the Retirement System's office at 23295 Schoenherr, Warren, MI 48089, (586) 774-6564.

City of Warren Police and Fire Retirement System

Statement of Plan Net Assets December 31, 2003

Assets

Cash (Note 5)	\$	101,089
Due from City of Warren - General Fund		150,216
Accrued interest and dividends receivable		1,087,197
Investments (Note 5):		
Category 3:		
U.S. government obligations		16,483,085
U.S. government agencies notes and debentures		24,316,699
Corporate and other bonds and securities		31,280,006
Equities		<u>166,374,921</u>
Total Category 3 investments		238,454,711
Noncategorized:		
Securities lending short-term collateral bank investment pool		31,208,030
Short-term cash management funds		5,345,585
Distressed debt recovery fund		1,636,015
Equity mutual funds		7,761,134
Fixed income mutual funds		3,018,893
Real estate investment trusts		<u>8,254,795</u>
Total investments		<u>295,679,163</u>
Total assets		297,017,665

Liabilities

Due to City of Warren - General Fund		99,845
Amounts due broker under securities lending agreement		31,208,030
Accounts payable:		
Money managers - Net		104,582
Other		<u>31,962</u>
Total liabilities		<u>31,444,419</u>

Net Assets Held in Trust for Pension Benefits - A schedule of funding progress is presented in the additional information

\$ 265,573,246

City of Warren Police and Fire Retirement System

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

Additions

Interest and dividends	\$ 6,314,484
Net appreciation in fair value of investments	42,921,306
Less investment expenses	<u>(1,288,547)</u>
Net investment income	47,947,243
Securities lending income:	
Interest and fees	486,190
Less borrower rebates and bank fees	<u>(421,690)</u>
Net securities lending income	64,500
Contributions:	
Employee contributions	375,025
Employer contributions	149,553
Employer contributions made on behalf of employees (Note 3)	<u>1,148,042</u>
Total additions	49,684,363

Deductions

Retirees' pension benefits	13,772,426
Member refunds and withdrawals	848,659
Administrative expenses	<u>229,028</u>
Total deductions	<u>14,850,113</u>

Net Increase

34,834,250

Net Assets Held in Trust for Pension Benefits

Beginning of year	<u>230,738,996</u>
End of year	<u><u>\$ 265,573,246</u></u>

City of Warren Police and Fire Retirement System

Notes to Financial Statements December 31, 2003

Note 1 - Significant Accounting Policies

The City of Warren Police and Fire Retirement System (the "System") is the administrator of a single-employer public employees' retirement system that covers substantially all police and fire employees of the City of Warren, Michigan. The financial statements of the System are also included in the combined financial statements of the City of Warren (the "City") as a pension trust fund.

Basis of Accounting - The System's financial statements are prepared using the accrual basis of accounting. Employee and employer contributions are recognized as revenue in the period in which employee services are performed. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Method Used to Value Investments - Investments are reported at fair value. Securities traded on a national exchange are valued at the last reported sales price.

Note 2 - Plan Description

The System provides retirement, disability, and death benefits to plan members and their beneficiaries. The obligation to contribute to and maintain the System for these employees was established by City ordinance and negotiation with the police and fire collective bargaining units. At December 31, 2002, the date of the most recent actuarial valuation, membership consisted of 375 retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits but not yet receiving them, and 414 current active employees.

Note 3 - Contributions

The funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are intended to accumulate sufficient assets to pay pension benefits when due.

Police and fire employment contracts provide for direct employee pension contributions of 1 percent of payroll for all fire employees and for police employees hired prior to July 1, 2000 and 5 percent of payroll for all police employees hired after July 1, 2000. In addition, the agreements provide that City contributions, equal to 4 percent of payroll, be made on behalf of all fire employees and the police employees hired prior to July 1, 2000. Under the terms of the contracts, these employer contributions made on behalf of the employees are effectively treated as direct employee contributions and are, therefore, recorded in the reserved net asset balance for employee contributions.

Administrative costs of the plan are financed through investment earnings.

City of Warren Police and Fire Retirement System

Notes to Financial Statements December 31, 2003

Note 4 - Reserves

As of December 31, 2003, the System's legally required reserves have been fully funded as follows:

Reserve for employees' contributions	\$ 18,062,422
Reserve for retired benefit payments	140,715,874

Note 5 - Deposits and Investments

Deposits - As of December 31, 2003, the System had a bank deposit balance of \$104,179 in the general account.

Investments - The System is authorized by Michigan Public Act 485 of 1996 to invest in U.S. bonds and notes, certain commercial paper, U.S. government repurchase agreements, bankers' acceptances, mutual funds, investment pools that are composed of authorized investment vehicles, certain reverse repurchase agreements, stocks, diversified investment companies, annuity investment contracts, real estate leased to public entities, mortgages, debt or equity of certain small businesses, certain state and local government obligations, and certain other specified investment vehicles. At December 31, 2003, there were no investments in any one organization (other than the U.S. government) in excess of 5 percent of net assets available for benefits.

The System's investments are categorized in the financial statements to give an indication of the level of risk assumed by the System at December 31, 2003. Category 1 includes investments that are insured or registered or for which the securities are held by the System or its agent in the System's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the System's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or agent, but not in the System's name. Except for the noncategorized investments, discussed subsequently, the System's investments at December 31, 2003 were classified as Category 3.

Short-term cash management funds (consisting primarily of bank investment pools), mutual funds, and real estate investment trusts are not categorized because they are not evidenced by securities that exist in physical or book entry form. All external investment pools are registered with the SEC. Management believes that the investments in the bank investment pools comply with the investment authority noted above.

City of Warren Police and Fire Retirement System

Notes to Financial Statements December 31, 2003

Note 5 - Deposits and Investments (Continued)

Included in the System's investments at December 31, 2003 are the following:

Asset-backed securities of approximately \$2,700,000. These securities are backed by credit card or other receivables and typically include credit enhancements in the form of overcollateralization, third-party letters of credit, seller recourse, insurance company guarantees, and/or senior subordinated structures. These securities are generally considered to offer moderate credit risk, but such risk varies depending on the type of asset being securitized and the extent and nature of the credit enhancement. Prepayment of these "pay through" securities could result in difficulty reinvesting the prepaid amounts in investments with comparable yields.

U.S. government agency collateralized mortgage obligations and pools of approximately \$11,000,000. Except for approximately \$500,000 issued by the Government National Mortgage Association, these investments are not backed by the full faith and credit of the U.S. government, but are generally considered to offer modest credit risks. The yields provided by these mortgage-related securities historically have exceeded the yields on other types of U.S. government securities with comparable maturities, in large measure due to the potential for prepayment. Prepayment could result in difficulty in reinvesting the prepaid amounts in investments with comparable yields.

As permitted by state statutes, and under the provisions of securities lending authorization agreements, the System lends securities to broker-dealers and banks for collateral that will be returned for the same securities in the future. The System's securities custodians manage the securities lending program and receive cash, government securities, or irrevocable bank letters of credit as collateral. Borrowers are required to deliver collateral for each loan of not less than 100 percent of the market value of the loaned securities. During the year ended December 31, 2003, only United States currency was received as collateral.

The System did not impose any restrictions during the fiscal year on the amount of loans made on its behalf by the securities custodians. There were no failures by any borrowers to return loaned securities or pay distributions thereon during the fiscal year. Moreover, there were no losses during the fiscal year resulting from a default of the borrowers or securities custodians.

City of Warren Police and Fire Retirement System

Notes to Financial Statements December 31, 2003

Note 5 - Deposits and Investments (Continued)

All securities loans can be terminated on demand by either the System or the borrower. The cash collateral received on each loan was invested, together with the cash collateral of other lenders, in an investment pool. The average duration of the investments held by the investment pool as of December 31, 2003 was 116 days. Because loans are terminable on demand, their duration did not generally match the duration of the investments made with cash collateral. On December 31, 2003, the System had no credit risk exposure to borrowers. The collateral held and the fair market value of underlying securities on loan for the System as of December 31, 2003 were \$31,208,030 and \$30,268,548, respectively.

Note 6 - Risk Management

The System's exposure to risks of loss, other than investment market loss, is minimal. Exposure is limited primarily to errors and omissions. The System has commercial insurance for such claims. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

Required Supplementary Information

City of Warren Police and Fire Retirement System

Required Supplementary Information Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Overfunded AAL (b-a)	Funded Ratio (Percentage) (a/b)	Valuation Payroll	Unfunded AAL as a Percentage of Valuation Payroll
12/31/97	\$ 220,594,836	\$ 209,333,909	\$ (11,260,927)	105.38	\$ 25,312,595	-
12/31/98	258,041,612	220,079,029	(37,962,583)	117.25	25,335,964	-
12/31/99	291,279,446	230,109,735	(61,169,711)	126.58	25,814,862	-
12/31/00	315,902,368	230,836,429	(85,065,939)	136.85	26,048,853	-
12/31/01	322,076,923	249,131,827	(72,945,096)	129.28	28,469,158	-
12/31/02	305,839,164	254,162,580	(51,676,584)	120.33	28,352,146	-

City of Warren Police and Fire Retirement System

Required Supplementary Information Schedule of Employer Contributions

The information presented above was determined as part of the actuarial valuations at the dates indicated. Additional information as of December 31, 2002, the latest actuarial valuation date, follows:

Actuarial cost method	Entry age
Amortization method	Level percentage of payroll
Remaining amortization period	13 years
Asset valuation method	Four-year smoothed market
Actuarial assumptions:	
Investment rate of return	7.5%
Projected salary increases*	0.1%-3.0%
*Includes inflation at	5.0%
Cost of living adjustment	None

<u>Years Ended</u> <u>December 31</u>	<u>Annual Required</u> <u>Contribution</u>	<u>Percentage</u> <u>Contributed</u>
1998	\$ 6,142,905	100.00
1999	5,976,610	100.00
2000	6,211,651	100.00
2001	6,190,998	100.00
2002	3,704,792	100.00
2003	1,297,595	100.00